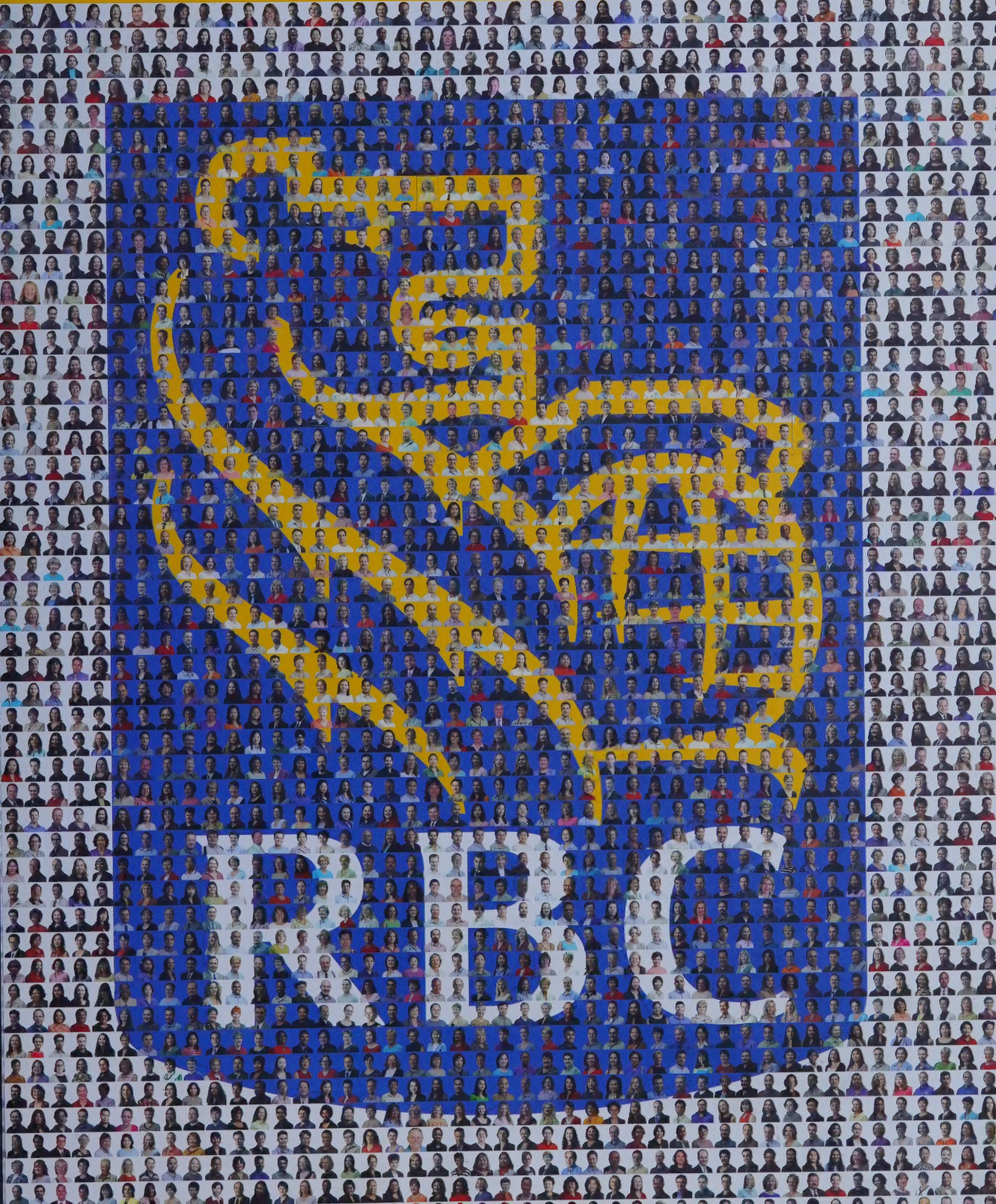


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University of Alberta
118 Business Building
Edmonton, Alberta T6G 2R6

BUILDING ON OUR STRENGTHS



Corporate profile

Royal Bank of Canada (RBC), which trades as RY on the TSX and NYSE, and its subsidiaries operate under the masterbrand RBC Financial Group, and has five major lines of business: personal and commercial banking (RBC Banking), wealth management (RBC Investments), insurance (RBC Insurance), corporate and investment banking (RBC Capital Markets) and securities custody and transaction processing (RBC Global Services). RBC is one of North America's premier diversified financial services companies and Canada's largest company as measured by assets and market capitalization. In total, we serve more than 12 million personal, business and public sector clients worldwide from offices in more than 30 countries.

In Canada, we have strong positions in all lines of business. In personal and commercial banking, we rank first or second in most retail products including mortgages and deposits. In wealth management, we have the leading full-service brokerage operation (by assets), the largest private bank, the top mutual fund provider among Canadian banks and the second-largest self-directed brokerage operation (by accounts). In corporate and investment banking, we continue to be the top-ranked securities underwriter and a leading mergers & acquisitions (M&A) advisor. We are the largest Canadian bank-owned insurer, one of the fastest growing in the country, and a leader in travel insurance and creditor products. We also have by far the largest custody operations in the country. Our domestic delivery network includes 1,311 branches and other units, and 4,151 banking machines. Currently, we have 2.3 million online and 2.4 million telephone clients.

In the United States, we provide personal and commercial banking, mortgage origination, insurance, full-service brokerage and corporate and investment banking services to over two million clients through RBC Centura, RBC Mortgage, RBC Builder Finance, RBC Liberty Insurance, RBC Dain Rauscher and RBC Capital Markets. Outside North America, we provide corporate and investment banking, trade finance, correspondent banking, treasury and securities custody services to business clients, and private banking services to individuals. We also have a retail network in the Caribbean and the Bahamas and a major presence in the global reinsurance market.

Vision

To be a leading North American financial services organization, pre-eminent in Canada, with specialized global businesses in those areas where we have a strong competitive position.

Values

- Excellent service to clients and each other
- Working together to succeed
- Personal responsibility for high performance
- Diversity for growth and innovation
- Trust through integrity in everything we do

Goals

- To be recognized as:
 - The undisputed lead provider of integrated financial services in Canada
 - A best in class provider of select financial services in the United States
 - A premier provider of specialized global financial services

Strategic priorities

- Strong fundamentals
- North American expansion
- Growth of high-return or high-P/E multiple businesses
- Cross-platform leverage

| | | | | | | | |
|---|------------------------------------|----|----------------------------|-----|----------------------------------|-----|----------------------------------|
| 1 | Financial highlights | 9 | North American expansion | 21 | Financial review (U.S. GAAP) | 105 | Directors and executive officers |
| 2 | Chairman's message | 13 | Growth of our businesses | | | 106 | Corporate governance |
| 3 | Chief Executive Officer's message | 16 | Cross-platform leverage | 21A | Financial review (Canadian GAAP) | 108 | Principal subsidiaries |
| 8 | Performance compared to objectives | 18 | Frequently asked questions | 103 | Glossary | IBC | Shareholder information |
| | | 20 | Serving our stakeholders | | | | |

Financial highlights ⁽¹⁾

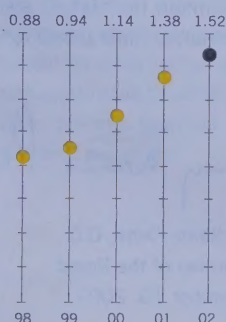
| (C\$ millions, except per share, number and percentage amounts) | Change 2002/2001 | 2002 | 2001 | 2000 | 1999 | 1998 |
|---|---------------------|------------|------------|------------|------------|------------|
| Earnings | | | | | | |
| Net interest income (2) | 10% | \$ 7,191 | \$ 6,529 | \$ 5,307 | \$ 5,152 | \$ 5,101 |
| Non-interest revenue | 5 | 8,579 | 8,155 | 6,680 | 5,491 | 4,997 |
| Gross revenues (2) | 7 | 15,770 | 14,684 | 11,987 | 10,643 | 10,098 |
| Provision for credit losses | (5) | 1,065 | 1,119 | 691 | 760 | 575 |
| Non-interest expense | 6 | 10,244 | 9,641 | 7,628 | 7,141 | 6,510 |
| Net income | 19 | 2,898 | 2,435 | 2,208 | 1,725 | 1,772 |
| Core net income (3) | 30 | 2,898 | 2,231 | 2,208 | 1,813 | 1,789 |
| Return on common equity (ROE) | — | 16.6% | 16.6% | 19.3% | 15.3% | 17.6% |
| Core ROE (3) | 150 bp | 16.6 | 15.1 | 19.3 | 16.1 | 17.8 |
| Economic Profit (4) | 44% | \$ 838 | \$ 583 | \$ 714 | \$ 337 | \$ 461 |
| Balance sheet data | | | | | | |
| Loans (before allowance for loan losses) | —% | \$ 171,523 | \$ 171,177 | \$ 156,184 | \$ 144,793 | \$ 146,772 |
| Assets | 5 | 381,932 | 362,483 | 294,054 | 273,298 | 281,074 |
| Deposits | 4 | 245,040 | 235,687 | 206,237 | 187,897 | 180,005 |
| Subordinated debentures | 1 | 6,960 | 6,861 | 5,825 | 4,596 | 4,087 |
| Common equity | 6 | 17,240 | 16,215 | 11,296 | 10,435 | 9,748 |
| Capital ratios (Canadian basis) (5) | | | | | | |
| Common equity to risk-adjusted assets | 100 bp | 10.4% | 9.4% | 7.3% | 7.1% | 6.2% |
| Tier 1 capital | 60 | 9.3 | 8.7 | 8.6 | 8.1 | 7.4 |
| Total capital | 90 | 12.7 | 11.8 | 12.0 | 11.2 | 10.5 |
| Capital ratios (U.S. basis) (6) | | | | | | |
| Common equity to risk-adjusted assets | 100 | 10.5 | 9.5 | 7.2 | 7.0 | 6.1 |
| Tier 1 capital | 40 | 8.5 | 8.1 | 7.8 | 7.6 | 6.8 |
| Total capital | 70 | 11.9 | 11.2 | 11.3 | 10.7 | 10.1 |
| Common share information | | | | | | |
| Shares outstanding (in thousands) | | | | | | |
| End of year | (1)% | 665,257 | 674,021 | 602,398 | 617,768 | 617,581 |
| Average basic | 5 | 672,571 | 641,516 | 606,389 | 626,158 | 617,324 |
| Average diluted | 5 | 679,153 | 647,216 | 609,865 | 632,305 | 633,626 |
| Earnings per share | | | | | | |
| Basic | 16 | \$ 4.16 | \$ 3.58 | \$ 3.42 | \$ 2.50 | \$ 2.64 |
| Diluted | 16 | 4.12 | 3.55 | 3.40 | 2.48 | 2.58 |
| Core diluted (3) | 27 | 4.12 | 3.24 | 3.40 | 2.63 | 2.61 |
| Share price | | | | | | |
| High (7) | 11 | 58.89 | 53.25 | 48.88 | 42.13 | 46.10 |
| Low (7) | 8 | 45.05 | 41.60 | 27.25 | 29.65 | 28.75 |
| Close | 16 | 54.41 | 46.80 | 48.30 | 31.73 | 35.55 |
| Dividends per share | 10 | 1.52 | 1.38 | 1.14 | 0.94 | 0.88 |
| Book value per share — year-end | 8 | 25.91 | 24.06 | 18.75 | 16.89 | 15.78 |
| Market capitalization (\$ billions) | 15 | 36.2 | 31.5 | 29.1 | 19.6 | 22.0 |
| Number of: | | | | | | |
| Employees (full-time equivalent) | 1,981 | 59,549 | 57,568 | 49,232 | 51,891 | 51,776 |
| Automated banking machines | (59) | 4,486 | 4,545 | 4,517 | 4,585 | 4,317 |
| Service delivery units | | | | | | |
| Canada | (6) | 1,311 | 1,317 | 1,333 | 1,410 | 1,422 |
| International | 83 | 807 | 724 | 306 | 99 | 106 |

- (1) Financial information is derived from U.S. GAAP consolidated financial statements, unless otherwise noted. Select definitions are available in the Glossary on pages 103 and 104.
 (2) Taxable equivalent basis.
 (3) Core results exclude special items, special items for 2001 are shown in Table 6 on page 27.
 (4) Economic Profit is cash operating earnings (i.e., net income available to common shareholders excluding the after-tax impact of special items and amortization of goodwill and other intangibles) less a charge for the cost of common equity. For more detail on Economic Profit, see page 26.
 (5) Using guidelines issued by the Superintendent of Financial Institutions Canada (OSFI) and Canadian GAAP financial information.
 (6) Using guidelines issued by the Board of Governors of the Federal Reserve System in the U.S. and U.S. GAAP financial information.
 (7) Intraday high and low share prices.

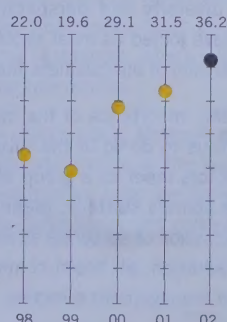
**Core diluted earnings
per share (C\$)**



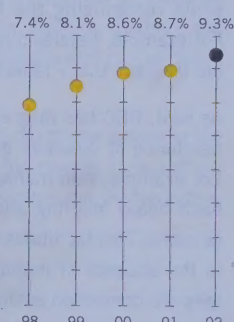
**Dividends
per share (C\$)**



**Market capitalization
(C\$ billions)**



**Tier 1 capital ratio
(Canadian basis)**



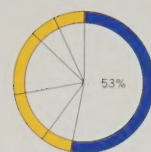


A STRONG AND DIVERSIFIED BUSINESS

Business profile

RBC Banking serves over 11 million individuals, small and medium-sized businesses, and mid-market commercial clients in Canada, the U.S., the Caribbean and the Bahamas. Distribution capabilities include a network of branches, business banking centres and other sales units, accredited financial planners, mobile sales representatives, automated banking machines, and telephone and Internet banking channels. Financial services include deposit accounts, investments and mutual funds, financial planning and advice, credit and debit cards, business and personal loans, and residential and commercial mortgages.

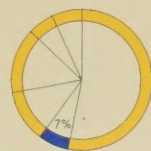
Share of RBC 2002 net income (1)



RBC Royal Bank (2)
RBC Centura (3)
RBC Mortgage (3)
RBC Builder Finance (3)
RBC Royal Bank of Canada (4)



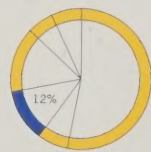
RBC Insurance provides a wide range of creditor, life, health, travel, home, auto and reinsurance products and services to more than five million clients in Canada, the U.S. and internationally. These products and services are offered through a wide variety of distribution channels, including the telephone, independent brokers, travel agents, a proprietary sales force and the Internet.



RBC Insurance (5)
RBC Liberty Insurance (3)



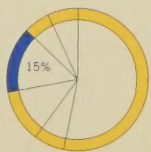
RBC Investments provides full-service and self-directed brokerage, financial planning, investment counselling, personal trust, private banking and investment management products and services primarily to private clients in Canada, the U.S. and internationally. Products and services are delivered through RBC Royal Bank's branch network across Canada, RBC Investments offices, RBC Dain Rauscher branches in the U.S., private banking offices and other locations worldwide. Services are also delivered via the Internet and telephone.



RBC Investments (5)
RBC Dain Rauscher (3)
RBC Global Private Banking (5)



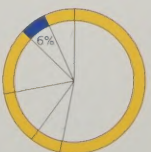
RBC Capital Markets provides wholesale financial services to large corporate, government and institutional clients in North America and in specialized product and industry sectors globally. Headquartered in Toronto, RBC Capital Markets has key centres of expertise in Minneapolis, New York and London, and offices in 27 other cities.



RBC Capital Markets (5)



RBC Global Services offers specialized transaction processing services to business, commercial, corporate and institutional clients in domestic and select international markets. Key businesses include investment administration, correspondent banking, cash management, payments and trade finance. Our 50 per cent interest in the Moneris Solutions merchant card processing joint venture is reported under RBC Global Services.



(1) Another 7% of net income was derived from the Other segment.
(2) Canadian brand name.
(3) U.S. brand name.
(4) Caribbean and the Bahamas brand name.
(5) Global brand names.

Strategic highlights

- Ensure strong revenue growth in Canada by maximizing client retention, deepening client relationships, capturing inter-generational wealth transfer and building on our financial planning and advice capabilities
- Accelerate U.S. revenue and earnings growth by expanding our footprint in the southeastern U.S. and building a scalable platform

- Ensure as many RBC clients as possible have an insurance relationship with RBC Insurance
- Continue to expand in the U.S. by utilizing existing scale and expanding the platform, entering new markets and focusing on cross-platform initiatives
- Build an integrated North American insurance platform by leveraging cross-border synergies where permitted

- Seek lifelong and intergenerational relationships with clients in Canada by offering products and services for each stage of their wealth management needs
- Grow in the U.S. by broadening and deepening relationships with existing clients as well as through targeted acquisitions over time in order to generate greater market share and scale

- Maintain our position as a leading full-service provider in all of our markets in Canada by continuing to leverage our long-standing client relationships; our trading, research and sales capabilities; and the strength of our brand and reputation
- In the U.S., provide value-added solutions by offering clients a broad product portfolio delivered through specialized industry teams

- Build upon existing client relationships to develop new business in select domestic and international markets
- Grow through key alliances, acquisitions and partnerships; continue to leverage the Moneris Solutions joint venture
- Drive revenue growth by developing new products and selling higher-margin value-added services

Key operating highlights

- First financial institution to offer automotive dealers and independent leasing/daily rental companies capacity to process transactions online
- Introduced a redesigned Online Banking service, offering new features and enhancements to 2.3 million online clients
- Awarded top honours in *Investment Executive's* 2002 Account Managers' Report Card

- Expanded across Canada, opening five new life business development offices and four new career sales offices
- Introduced a new critical illness insurance product for Canada
- Announced a new term life insurance product for the U.S.

- Introduced new services for clients of RBC Action Direct: Fixed Income Online and Asset Mix calculator
- RBC Dain Rauscher's Fixed Income business was strong across both the municipal and taxable arenas in 2002

- Made substantial progress in building a strong business among U.S. mid-market clients
- Maintained our leading position in Canada, ranking number one or two in virtually every business according to published league tables
- Launched the Alternative Investments division in response to client needs for non-traditional opportunities to diversify their long-term investment portfolios

- Won a number of custody mandates, including those awarded by Mackenzie Financial Corporation and AIM Funds Management, Inc., and expanded CI Mutual Funds Inc., outsourcing agreements
- Performed strongly in key international client satisfaction surveys
- Developed and marketed a nostro service to settle Canadian dollar transactions for Continuous Linked Settlement

Core financial highlights (6) – U.S. GAAP

| (C\$ millions, taxable equivalent basis, except percentage amounts) | % change | 2002 | 2001 |
|---|----------|----------|----------|
| Gross revenues | 6% | \$ 7,666 | \$ 7,215 |
| Non-interest expense | 5 | 4,520 | 4,297 |
| Net income | 22 | 1,546 | 1,270 |
| Economic Profit | 47 | 614 | 419 |
| Return on equity | 90 bp | 19.2% | 18.3% |

| (C\$ millions, except percentage amounts) | % change | 2002 | 2001 |
|---|----------|--------|--------|
| Gross revenues | 7% | \$ 580 | \$ 542 |
| Non-interest expense | 6 | 399 | 375 |
| Net income | 10 | 190 | 173 |
| Economic Profit | 39 | 100 | 72 |
| Return on equity | 570 bp | 25.7% | 20.0% |

| (C\$ millions, except percentage amounts) | % change | 2002 | 2001 |
|---|----------|----------|----------|
| Gross revenues | 26% | \$ 3,647 | \$ 2,894 |
| Non-interest expense | 25 | 3,144 | 2,510 |
| Net income | 48 | 346 | 234 |
| Economic Profit | (114) | (14) | 97 |
| Return on equity | (80)bp | 11.1% | 11.9% |

| (C\$ millions, taxable equivalent basis, except percentage amounts) | % change | 2002 | 2001 |
|---|----------|----------|----------|
| Gross revenues | (3)% | \$ 2,695 | \$ 2,781 |
| Non-interest expense | (10) | 1,627 | 1,804 |
| Net income | 17 | 439 | 376 |
| Economic Profit | (25) | (55) | (44) |
| Return on equity | – | 10.5% | 10.5% |

| (C\$ millions, except percentage amounts) | % change | 2002 | 2001 |
|---|----------|--------|--------|
| Gross revenues | 5% | \$ 808 | \$ 769 |
| Non-interest expense | 13 | 548 | 485 |
| Net income | (8) | 173 | 189 |
| Economic Profit | (18) | 100 | 122 |
| Return on equity | (600)bp | 28.7% | 34.7% |

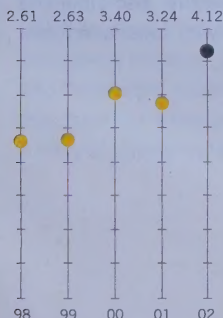
(6) Excluding special items in 2001 detailed in Table 6 on page 27.

Financial highlights ⁽¹⁾

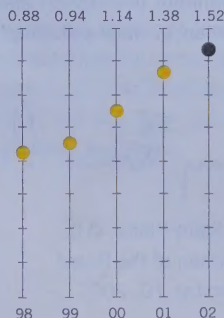
| (C\$ millions, except per share, number and percentage amounts) | Change 2002/2001 | 2002 | 2001 | 2000 | 1999 | 1998 |
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| Capital ratios (Canadian basis) (5) | | | | | | |
| Common equity to risk-adjusted assets | 100 bp | 10.4% | 9.4% | 7.3% | 7.1% | 6.2% |
| Tier 1 capital | 60 | 9.3 | 8.7 | 8.6 | 8.1 | 7.4 |
| Total capital | 90 | 12.7 | 11.8 | 12.0 | 11.2 | 10.5 |
| Capital ratios (U.S. basis) (6) | | | | | | |
| Common equity to risk-adjusted assets | 100 | 10.5 | 9.5 | 7.2 | 7.0 | 6.1 |
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| Earnings per share | | | | | | |
| Basic | 16 | \$ 4.16 | \$ 3.58 | \$ 3.42 | \$ 2.50 | \$ 2.64 |
| Diluted | 16 | 4.12 | 3.55 | 3.40 | 2.48 | 2.58 |
| Core diluted (3) | 27 | 4.12 | 3.24 | 3.40 | 2.63 | 2.61 |
| Share price | | | | | | |
| High (7) | 11 | 58.89 | 53.25 | 48.88 | 42.13 | 46.10 |
| Low (7) | 8 | 45.05 | 41.60 | 27.25 | 29.65 | 28.75 |
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| Dividends per share | 10 | 1.52 | 1.38 | 1.14 | 0.94 | 0.88 |
| Book value per share — year-end | 8 | 25.91 | 24.06 | 18.75 | 16.89 | 15.78 |
| Market capitalization (\$ billions) | 15 | 36.2 | 31.5 | 29.1 | 19.6 | 22.0 |
| Number of: | | | | | | |
| Employees (full-time equivalent) | 1,981 | 59,549 | 57,568 | 49,232 | 51,891 | 51,776 |
| Automated banking machines | (59) | 4,486 | 4,545 | 4,517 | 4,585 | 4,317 |
| Service delivery units | | | | | | |
| Canada | (6) | 1,311 | 1,317 | 1,333 | 1,410 | 1,422 |
| International | 83 | 807 | 724 | 306 | 99 | 106 |

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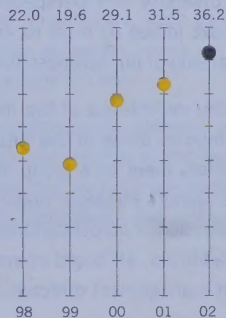
**Core diluted earnings
per share (C\$)**



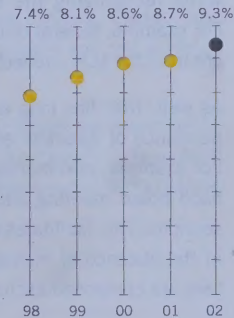
**Dividends
per share (C\$)**

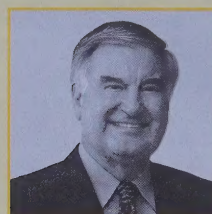


**Market capitalization
(C\$ billions)**



**Tier 1 capital ratio
(Canadian basis)**





GUY SAINT-PIERRE, O.C.
CHAIRMAN OF THE BOARD

I am pleased to report on behalf of Royal Bank of Canada's Board of Directors. This past year has been a tumultuous one in virtually every sector of the economy, marked with serious concerns about oversight and governance. In this environment, your board remains committed to sound corporate governance and transparent disclosure. We congratulate management and all RBC employees for their accomplishments and extraordinary efforts in meeting the challenges of 2002.

The public scrutiny and debate this past year provided the board with the opportunity to refine our governance standards and the satisfaction of seeing some of our own long-standing practices recognized by regulators and other observers as leading edge. Your board and management know we must remain vigilant in fostering and reinforcing a culture of governance and integrity throughout RBC – starting at the very top.

The foundation of RBC's corporate governance process includes a majority independent board with an independent chairman and knowledgeable, well-informed directors who give priority to strategic planning. They ensure that standards exist to promote ethical behaviour throughout the organization while constantly striving to improve corporate governance practices.

We place considerable importance on the process of nominating directors. In seeking candidates with the qualities essential to the leadership of a highly competitive and complex global business, the Corporate Governance and Public Policy Committee focuses on the specific needs of RBC and its strategic direction, while recognizing the benefits of diversity and perspective. For example, several directors who have joined us most recently are from the U.S. – reflecting the expansion of our business there.

As well, RBC has long emphasized the importance of the independence of directors and will continue to do so in the future. For example, non-management directors meet as a group after each board meeting and during the board's strategic planning sessions. This facilitates a candid discussion of corporate strategy in the absence of management. In addition, all board committees are composed exclusively of non-management directors.

Access to information is also critical to your board's strength and independence. RBC has an orientation program for new directors and undertakes ongoing education programs. RBC also ensures that the board has timely access to information it needs to make decisions, and free and open access to any and all members of management.

These and other strengths are rooted in a commitment to continuous improvement in corporate governance. RBC keeps close watch on changes in the business and regulatory environment and monitors governance initiatives in Canada and elsewhere, assessing its practices against them and adapting as appropriate. This enables the board to anticipate and implement beneficial changes as a matter of best practice, rather than merely as a response to regulatory or other external requirements.

As Chairman and a shareholder, I am pleased with the leadership RBC has shown in all aspects of its operations, financial performance and corporate governance. Along with my fellow directors, I am committed to working closely with management to maintain the highest standards of integrity, discipline and governance, while providing shareholders with superior returns.

Guy Saint-Pierre, O.C.
Chairman of the Board
December 10, 2002



GORDON M. NIXON
PRESIDENT & CHIEF
EXECUTIVE OFFICER

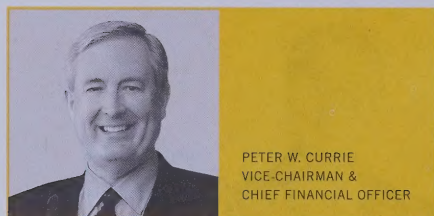
I am pleased to report that, in an environment marked by ongoing concerns about global economic growth, financial market uncertainty and geopolitical tensions, we generated record net income for our shareholders this past year totalling \$2.9 billion. While adjusting our businesses to perform well in the short term, we also continued to expand our capabilities and position ourselves for sustained long-term growth and consistent performance.

We have a number of strengths that we continued to build upon this year. Our diversification by business and geography tends to stabilize our returns and reduce earnings volatility. In Canada, we also have leading positions in most businesses, a large base of about 10 million clients and a very strong brand. This gives us the opportunity to deepen relationships with our existing clients and expand our business with them by offering a full suite of competitive products and services. In addition, we have a disciplined growth strategy. We have created a solid foundation in the United States, comprising personal and commercial banking, full-service brokerage, insurance and equity capital markets operations, and these businesses collaborated further with each other and with their Canadian partners this year to enhance the client experience, grow the business and realize efficiencies. We also have a record of solid and consistent financial performance and shareholder value creation. Shareholders have benefited not only from our share price appreciation, but also from our long history of uninterrupted and rising dividend payments.

Our goals

Our three key goals are to be recognized as the undisputed lead provider of integrated financial services in Canada, a best in class provider of select financial services in the U.S. and a premier provider of specialized global financial services. In Canada, we are committed to retaining our strong positions in all our businesses and offering our services on an integrated basis so we can provide better service and value to our clients. In the U.S., we want to focus on growing select areas, such as personal and commercial banking and wealth management, where we believe we have a competitive advantage and can offer best in class services. Outside North America, we will continue to focus on those businesses, such as global private banking, custody and foreign exchange, where we are strong globally and can generate attractive returns.

Our vision, goals, strategic priorities and values are shown in the corporate profile at the beginning of this report. It is against these that we base our decisions and measure our performance, both individually and collectively.



Our strategic priorities

To achieve our goals, we have established four key priorities – strong fundamentals, North American expansion, growth of high-return or high-P/E multiple businesses, and cross-platform leverage.

Strong fundamentals

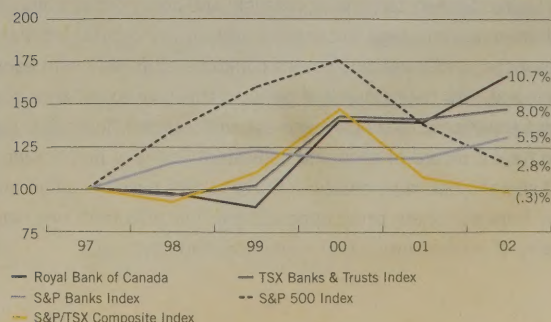
In 2002, we generated record net income of \$2.9 billion, up 19 per cent from 2001. Excluding special items and the amortization of goodwill last year, net income was up 17 per cent and earnings per share were 13 per cent higher.

Our aim is to maintain financial performance in the top quartile of North American financial companies and to meet or exceed our own objectives. As shown on page 8, we performed strongly this past year compared to almost all of our objectives – growing both revenues and earnings per share at a double-digit pace, continuing to demonstrate cost and asset quality discipline, enhancing our capital ratios and maintaining top quartile valuation. Our common share price rose 16 per cent in 2002, compared to a return of 1 per cent for the TSX Banks & Trusts Index over that same period.

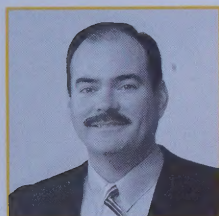
Our objectives for 2003 are similar to those we strived for in 2002, with the exception of the revenue growth goal, which we have lowered to 5–8 per cent from last year's 7–10 per cent, which had included a full year of revenues for RBC Centura, acquired seven months into 2001. In addition, we have raised the earnings per share growth objective to 10–15 per cent, reflecting our aim of increasing revenues at a faster rate than expenses and our expectation that capital market activity will pick up somewhat in 2003.

We have also modified some of our medium-term goals. With our strong commitment to shareholder value, we have raised our dividend payout goal from 30–40 per cent to 35–45 per cent. Our payout ratio this past year was 37 per cent and we raised our common share dividends by 10 per cent during the year. We also increased our Tier 1 capital ratio goal to 8–8.5 per cent from 8 per cent. Finally, we are raising our specific provision for credit losses ratio goal to .35–.45 per cent from .30–.40 per cent, in recognition of continuing economic uncertainty and expected growth in the personal, credit card and small business loan portfolios, which have loss ratios above the earlier goal range.

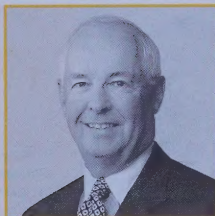
Five-year compound annualized total return (1)
October 31, 1997–October 31, 2002



(1) In Canadian dollars, assuming dividends are reinvested.



MARTIN J. LIPPERT
VICE-CHAIRMAN
RBC GLOBAL SERVICES
& CHIEF INFORMATION
OFFICER



W. REAY MACKAY
VICE-CHAIRMAN
RBC INVESTMENTS

North American expansion

One of our important objectives for 2002 was to enhance the performance of our recent U.S. acquisitions. These acquisitions contributed 21 per cent of total revenues in 2002, up from 12 per cent a year ago, and generated net income of \$232 million, up from \$(23) million on a core basis last year. This reflects the cessation of goodwill amortization expense this year, a full year of results and stronger performance at RBC Centura, the benefits of integrating Tucker Anthony Sutro Corporation into RBC Dain Rauscher and strong results from RBC Dain Rauscher's fixed income operations. RBC Dain Rauscher generated profit of \$3 million in 2002 versus a loss of \$73 million in 2001. Its retention compensation expenses will fall in 2003, further aiding performance.

We also aimed to limit U.S. acquisitions to a total purchase price of \$1 billion in 2002, in order to focus our efforts on integrating and leveraging our earlier acquisitions. We succeeded, announcing four small acquisitions for US\$610 million. Two are in personal and commercial banking (Eagle Bancshares, Inc. and Admiralty Bancorp, Inc.) and these will allow us to develop a presence in the high-growth Atlanta and Florida markets with a small number of well-located branches, a client base, banking licenses and good management. The Admiralty Bancorp acquisition is expected to close in early 2003. We intend to complement these small acquisitions with new branch expansion in high-growth regions in the southeastern U.S.

Each of our acquired U.S. companies is attempting to grow revenues and enhance efficiency not only on its own but also by working closely with the Canadian operations of its own platform and with its sister divisions in the U.S. As an example, RBC Liberty Insurance has launched a life specialist initiative,

a referral sales operation targeting clients of RBC Centura with 19 insurance specialists operating in North Carolina banking centres.

We are on our way to establishing a focused growth platform in the U.S., and detailed discussion of our North American expansion efforts is provided on pages 9–12.

Growth of high-return or high-P/E multiple businesses

We are focused on growing those businesses that have high returns, good growth prospects and attractive P/E multiples. Two areas we have targeted for the greatest long-term expansion are RBC Banking and RBC Investments, although other segments also have priority areas they are expanding. RBC Banking generates solid, consistent returns and we believe we can apply the principles which have supported our success in Canada, including our strong customer relationship management (CRM) capabilities, to the U.S. market. While the performance of RBC Investments has been dampened by the weakness in capital markets and client trading activity, the returns of this business in normal market conditions are strong and we are confident the long-term prospects for this business are good given demographic shifts and significant expected intergenerational wealth transfer.

As we have expanded our high-return businesses, we have continued to shrink low-return, capital-intensive and relatively volatile operations such as corporate lending. This contributed to a \$5.1 billion reduction in total business and government loans this past year. We have reduced risk-adjusted assets in our corporate loan book by approximately 30 per cent since 1998 and plan on further reductions.



JAMES T. RAGER
VICE-CHAIRMAN
RBC BANKING



IRVING WEISER
CHAIRMAN & CEO
RBC DAIN RAUSCHER

The benefits of our diversification, by business and geography, were apparent again in 2002. Close to 40 per cent of our core earnings growth this past year came from our recent U.S. acquisitions, demonstrating the benefit of geographic diversification. Also, despite continued economic uncertainty and weakness in capital markets, four of our five business platforms recorded double-digit core earnings growth. One-quarter of our earnings this year came from the relatively asset-quality immune businesses of RBC Insurance, RBC Investments and RBC Global Services.

Steps the business segments took this year to grow their operations are discussed on pages 13–15, while a detailed review of their financial performance and strategies is provided on pages 26–37.

Cross-platform leverage

This new strategic priority involves working across our various businesses and functions to share best practices, grow revenues by offering the products and services of one segment to the clients of another, and enhance efficiency by eliminating duplication. We have five very strong business segments and a large client base. By working together and offering integrated services to our clients, we believe we have a tremendous opportunity to grow our business and operate more efficiently. There are a number of initiatives underway across the organization that are focused on this priority, including the launch of RBC Referrals to better serve our clients and generate more business opportunities within RBC.

A detailed discussion of cross-platform leverage is provided on pages 16–17.

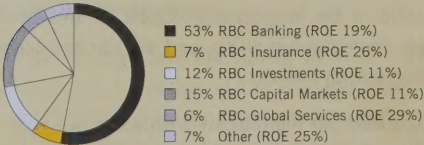
Commitment to our shareholders

While we have a record of significant shareholder value creation, we are by no means complacent. We will continue to target superior profitability and returns for our shareholders by continuing to pursue strategies and initiatives to grow our businesses profitably, manage our costs and risks effectively, and deploy our capital efficiently – reinvesting in our businesses and growth markets, and returning the excess to shareholders through share repurchases when appropriate as well as through dividend payments. The increase in our medium-term dividend payout goal attests to our commitment to rewarding shareholders.

Diversified business mix

25% of earnings from relatively asset-quality immune businesses (1)

NET INCOME CONTRIBUTION – 2002



(1) Asset-quality immune businesses include RBC Insurance, RBC Investments and RBC Global Services.



W. JAMES WESTLAKE
CHAIRMAN & CEO
RBC INSURANCE



CHARLES M. WINOGRAD
VICE-CHAIRMAN
RBC CAPITAL MARKETS

Corporate governance

This past year was marked by events in the corporate sector that led investors to seriously scrutinize the oversight and governance of companies. We have always attempted to be a leader in corporate governance and we will continue to strive for the highest standards in this area. We also made a number of refinements to our governance policies this past year, including changes relating to senior management and director compensation that took effect on November 1, 2002. We have also invested significant resources to ensure that our compliance and internal audit standards, policies and procedures represent best practices and that all parts of our organization live up to our values.

In addition to the comments from our Chairman on page 2, a discussion of corporate governance and board committee mandates and activities is provided on pages 106–107 and in our management proxy circular dated January 3, 2003, which includes details of senior management and director compensation.

Our employees

The strong results we recorded this past year reflect the tremendous dedication, commitment and hard work of our employees throughout RBC. Our people are our core strength. In 2002, we articulated five values key to RBC, shown in our corporate profile at the beginning of this report. These are embedded in the annual performance appraisal process for all our employees and will further inspire our people to provide excellent service and work together in a spirit of co-operation and trust for the benefit of our clients and shareholders.

Gordon M. Nixon
President & Chief Executive Officer
December 10, 2002

| 2002 objectives (1) | | 2002 performance (1) | 2003 objectives | Medium-term goals (3–5 year) |
|---|---|--|---|---|
| 1 Valuation Maintain top quartile valuation levels: | | | | |
| • Share price/book value: | 1st quartile of TSX Banks & Trusts Index | 1st quartile | 1st quartile of S&P/TSX Composite Banks Index (2) | N/A |
| • Share price/earnings: | 1st quartile of TSX Banks & Trusts Index | 1st quartile (3) | 1st quartile of S&P/TSX Composite Banks Index (2) | |
| Share price growth: | Above the TSX Banks & Trusts Index | Above the index | Above the S&P/TSX Composite Banks Index (2) | |
| 2 Earnings growth Grow diluted earnings per share by: | | | | |
| | 5–10% (4) | 27% (4) 13%, excluding goodwill amortization | 10–15% | 10–15% |
| 3 ROE Achieve an ROE of: | | | | |
| | 17–19% (4) | 16.6% (4) | 17–19% | 20%+ |
| 4 Revenue growth Achieve revenue growth of: | | | | |
| | 7–10% | 11% | 5–8% | 8–10% |
| 5 Expense growth Operating expenses versus operating revenues (5): | | | | |
| | Operating expense growth less than operating revenue growth | Operating expense growth 8%, compared to operating revenue growth of 11%. Excluding recent U.S. acquisitions, operating expenses down 5% and operating revenues flat | Operating expense growth less than operating revenue growth | N/A |
| 6 Portfolio quality Achieve a ratio of specific provisions for credit losses to average loans, acceptances and reverse repurchase agreements (6): | | | | |
| | .45–.55% | .51% .49% net of effect of credit derivatives (7) | .45–.55% | .35–.45% (was .30–.40%) |
| 7 Capital management Capital ratios (6): | | | | |
| | Maintain strong capital ratios | 9.3% Tier 1 capital ratio 12.7% Total capital ratio versus medium-term goals of 8% and 11–12%, respectively | Maintain strong capital ratios | 8–8.5% Tier 1 capital (was 8%) 11–12% Total capital |
| Dividend payout ratio (8) | | | | |
| | N/A | 37% | 35–45% | 35–45% (was 30–40%) |

(1) Excluding special items in 2001 (for growth in earnings, revenues and expenses) detailed on page 27.

(2) The TSX is discontinuing the TSX Banks & Trust Index in May 2003 and replacing it with the S&P/TSX Composite Banks Index.

(3) Computed by us on October 31, 2002, based on analysts' average core diluted earnings per share forward estimates for 2003.

(4) With the adoption in Q1/02 of new accounting standards regarding business combinations in Canada and the U.S., goodwill is no longer amortized. Accordingly, 2002 objectives for earnings growth and ROE are no longer on a "cash" basis, as reported earnings are now very similar to "cash" earnings.

(5) Operating expenses exclude special items, costs of Stock Appreciation Rights (SARs) and retention compensation associated with acquisitions, while operating revenues exclude special items.

(6) Calculated based on our Canadian GAAP financial statements.

(7) See discussion on page 46.

(8) Common share dividends as a percentage of net income after preferred dividends.



In 2000, we added North American expansion as a key strategic priority. We looked to markets outside Canada since the potential for future growth is limited by the size of that market and our already substantial market share there. Furthermore, we believe that our strengths in some Canadian businesses can be exported successfully, particularly into the U.S. The U.S. is the most logical market in which to expand – it's the largest global economy, a contiguous region, has similar culture and language to ours, and its banking sector offers good potential for growth.

Structurally, the U.S. financial services industry is fragmented, contains a number of monoline service providers and only recently began to move towards the provision of integrated financial services by diversified financial service companies. This is a significant opportunity for us as we have been successfully providing integrated financial services comprising banking, investment banking, brokerage, money management, custody and insurance on a nationwide basis for over a decade. By extending our banking, insurance and wealth management businesses into the U.S. through strategic acquisitions, we are ideally positioned to benefit from this growing trend.

Building a strong U.S. presence

Since April 2000, we have announced 10 U.S. acquisitions for US\$5.3 billion in total to lay the foundation for future growth. The 8 acquisitions that have closed have increased our total client base by approximately 2.3 million or 23 per cent in just 30 months with another approximate 170,000 expected upon the close of the Business Men's Assurance Company of America (BMA) and Admiralty Bancorp acquisitions. We have assembled a diversified platform in the U.S. with an emphasis on retail businesses – personal and commercial banking, wealth management and insurance – all businesses we know well and are very successful at in Canada. Our diversified approach reduces exposure to any one sector and provides us with the flexibility to adapt to changes in the business environment. This approach has helped us avoid significant earnings volatility in both Canada and the U.S. and represents one of our strengths.

We undertook each of our acquisitions because, among other criteria, our models indicated they would be accretive to cash earnings within three years. We have been successful in purchasing businesses that fit strategically, are manageable in size, generate healthy returns and possess strong management teams that share our culture, operating philosophy and aspiration for profitable growth.

The acquisitions of Centura Banks, Inc., Liberty Life Insurance Company, Liberty Insurance Services Corporation (LIS) and Dain Rauscher Corporation (Dain Rauscher), in the 2001 fiscal year, represented the first phase or the "platform extension" aspect of our U.S. expansion strategy. This phase entailed assembling the original building blocks of the businesses we wanted to extend into the U.S. Clearly, our expansion strategy has been a rollout, business line extension strategy, not a "bet-the-bank" strategy.

To assist clients in recognizing that these acquired businesses are all part of the RBC group, in 2001, we adopted a common branding, which uses the prefix RBC. At the same time, by retaining the Centura Banks and Dain Rauscher names, we are capitalizing on the strong brand equity and franchise value built over time by these firms in their local markets. To further enhance brand awareness, in September we acquired the naming right to the Entertainment and Sports Arena in Raleigh, N.C. – home of the National Hockey League's Carolina Hurricanes and North Carolina State University's National Collegiate Athletic Association (NCAA) men's basketball team. Under the terms of this 20-year agreement, the complex is now named the RBC Center.

Building a U.S. platform

U.S. acquisitions since April 2000



Executing Phase II of our U.S. expansion strategy

The second phase of our U.S. expansion consists of making follow-on acquisitions in personal and commercial banking and wealth management to realize cost synergies, expand geographic reach and client base in targeted areas, and to grow revenues. The first such acquisition was of Tucker Anthony Sutro, which closed on October 31, 2001. Its presence in California and the northeastern U.S. complemented RBC Dain Rauscher's presence in most of the remaining U.S., excluding the Southeast. The combination of Tucker Anthony Sutro and RBC Dain Rauscher virtually doubled the size of our U.S. wealth management platform, making it the ninth largest full-service brokerage firm in the U.S. with a national network of 142 brokerage offices in 39 states. Across North America, we now have approximately 3,400 financial consultants and advisors, 316 brokerage offices, \$270 billion in assets under administration and \$77 billion in assets under management. Further Phase II acquisitions were conducted in 2002, as described below.

Completed small, targeted acquisitions in 2002

We mentioned at the beginning of the year that we intended to limit our U.S. acquisitions in 2002 to \$1 billion in aggregate. And indeed, we announced four small targeted acquisitions totalling approximately US\$610 million.

In June, RBC Global Private Banking acquired the assets of Barclays Bank PLC's private banking business in the Americas, and the integration of the businesses began immediately. The total purchase premium offered was approximately US\$90 million, of which US\$45 million was paid at the time of closing of the transaction in 2002. The remaining amount to be paid will depend on the performance of the acquired business over the one-year period following the acquisition. As part of this transaction, we also acquired private banking on-balance sheet assets and liabilities with a net position of approximately US\$66 million. The client base of RBC Global Private Banking in the Americas region grew by approximately 10 per cent, with the addition of US\$2.9 billion of client assets consisting of discretionary investment management, investment advisory, trust and banking services. The addition of this business to our existing private banking operations fits with our strategy of growing our specialized global financial services. Clients are located mainly in the U.S., Latin America and the Caribbean. They will be served from RBC Global Private Banking offices in New York, Miami and Toronto, with linked international services from the Cayman Islands, London, Jersey and Geneva.

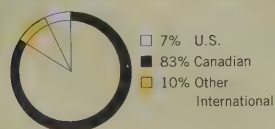
In July, RBC Centura completed its acquisition of Eagle Bancshares of Tucker, Georgia and its subsidiary, Tucker Federal Bank, for US\$149 million. Eagle Bancshares, with its 14 branches, provides us with a valuable presence in the attractive and high-growth metropolitan Atlanta market, provides a retail distribution channel to a high net worth market and further diversifies our U.S. retail network. Former Tucker Federal Bank branches are now operating as RBC Centura branches. We expect this transaction will yield integration cost savings of US\$7 million or 25 per cent of Eagle Bancshare's cost base and be accretive to earnings by the third quarter of 2003.

The following month, RBC Centura announced its proposed acquisition of Admiralty Bancorp, a Florida-based financial holding company with a commercial banking subsidiary, for approximately US\$150 million. This purchase further advances our expansion in the southeastern U.S. by securing a footprint in the lucrative and fast-growing southern and central Florida markets. Once this deal closes, which we expect in January 2003, Admiralty Bancorp's network of 10 branches in southern and central Florida will result in a total of 249 personal and commercial bank branches operating in 5 southeastern U.S. states. This purchase is expected to be accretive to earnings in fiscal 2005, in line with our objective of acquisitions being accretive in 2–3 years.

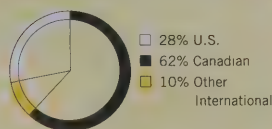
On the insurance side, RBC Insurance announced in April that it had reached an agreement to acquire certain assets of Generali Group, a Trieste, Italy-based insurer, comprising the operations of BMA and including an inforce block of approximately 150,000 traditional life insurance policies and annuities as well as the infrastructure for manufacturing variable insurance products. In a related transaction, RBC Dain Rauscher is planning to purchase Jones & Babson Inc., BMA's mutual fund company with US\$1.5 billion in assets under administration. These acquisitions are subject to regulatory approvals and approval by the board of directors and shareholders of the mutual funds, and other customary closing conditions.

Proportion of U.S. revenues growing

2000 REVENUES



2002 REVENUES



2002 achievements

In addition to small targeted acquisitions limited to no more than \$1 billion in total, our objectives for 2002 were to consolidate and enhance returns from earlier purchases through cost synergies and revenue growth initiatives. We met these objectives. Net income from U.S. acquisitions was \$232 million in 2002, up from a loss of \$80 million (a loss of \$23 million, excluding special items) a year ago. This improvement reflects a full year of results at RBC Centura, improved performance at RBC Dain Rauscher following the acquisition of Tucker Anthony Sutro, cessation of goodwill amortization, benefits attributable to the continued integration of our acquisitions, and our revenue enhancement and cost-saving initiatives. Our U.S. revenues have risen to 28 per cent of total revenues from just 7 per cent in 2000.

Strong performance at RBC Centura

In 2002, RBC Centura achieved net income of \$206 million, up from \$21 million in 2001, when five months of RBC Centura results were included. RBC Centura achieved approximately 97 per cent of the US\$70 million of cost savings targeted for mid-2004 by the end of 2002. The integration of Security First Network Bank (SFNB) into RBC Centura was finished faster and more efficiently than originally planned and the two former SFNB branches in Atlanta, Georgia and Largo, Florida now operate as RBC Centura branches. We have set aggressive 3-year growth goals for RBC Centura – 7–10 per cent growth in revenue and 2–5 per cent growth in non-interest expense, which translates into net income growth in the strong double digits.

Results improving at RBC Dain Rauscher

The third quarter of 2002 represented a turning point for RBC Dain Rauscher, which posted a profit of \$10 million during that quarter, reflecting cost reductions from the Tucker Anthony Sutro integration and good performance in fixed income operations. We have so far managed to achieve 50 per cent of the US\$60 million in targeted cost savings for this integration, with the remainder expected by the end of 2003. For the year, RBC Dain Rauscher posted net income of \$3 million, reflecting losses incurred during the first half of 2002, up from a loss of \$73 million in 2001. Retention compensation costs are expected to decline significantly in 2003, and register further reductions over the coming years. With its 2,000 financial consultants, following the very successful integration of Tucker Anthony Sutro, we believe RBC Dain Rauscher is right sized and poised to benefit from a market recovery.

RBC Liberty Insurance continues its progress

We extended our insurance platform into the U.S. with the acquisition of Liberty Life Insurance, LIS and certain assets of Genelco Incorporated in the 2001 fiscal year. These purchases provided us with capabilities in life insurance and insurance administration in the U.S. market. The pending acquisition of BMA will provide variable life and variable annuity capabilities. Liberty Life Insurance and LIS were purchased with little goodwill and earned US\$23 million in 2002 compared to US\$29 million in 2001. In May, RBC Liberty Insurance completed the migration and consolidation of its business process outsourcing and administration functions, from St. Louis, Missouri, which had been acquired from Genelco, to RBC Liberty Insurance's operations in Greenville, South Carolina – one month ahead of schedule.

Executing cross-platform leverage

As part of our cross-platform leverage strategic priority, we are assessing opportunities to enhance revenues and reduce costs through the elimination of overlap and improvements in operating efficiency both on a north-south basis within individual platforms and on an east-west basis across platforms in the U.S.

There are numerous examples of cross-platform leverage initiatives that have yielded favourable results. RBC Banking is continuing to export to the U.S. its Canadian expertise in sales practices and performance management as well as segment and product management. This has favourably impacted RBC Centura. Capacity and cost benefits have accrued from the use of Canadian call centres by RBC Centura and we have relocated data processing to Canada. The president of RBC Dain Rauscher, Peter Armenio, who formerly headed our Canadian brokerage platform, is working closely with Irv Weiser and our people in Canada to share best practices within RBC Investments across the border. And, RBC Insurance is sharing its Canadian market-leading creditor insurance expertise with RBC businesses in the U.S. For additional discussion of cross-platform leverage, see pages 16–17.

Future U.S. expansion

So, where do we go next in the U.S.? With approximately 3,400 financial consultants and investment advisors in North America, we are close to our medium-term target of 4,000. Future wealth management acquisitions over the short term will likely be small additions to our existing

base. Our focus will be on continuing to grow RBC Centura, with an emphasis on targeted purchases and new branch openings in the south-eastern U.S. However, there are a number of considerations that will impact our U.S. growth deliberations. First is the trade-off between our strong fundamentals and North American expansion priorities. In the short term, one inevitably compromises the former to achieve the latter. Still, despite the sizeable investments we've made in the U.S. and the current weak brokerage environment, we maintained a strong showing from the profitability standpoint in 2002. We intend to continue to do so. The second consideration is the identification of acquisitions that make sense from strategic, cultural and shareholder value creation perspectives. Although we are always on the lookout for potential acquisitions, we do not intend to invest unless the addition meets our financial and other requirements. Third, bank mergers in Canada will have implications not only for the Canadian franchise but also for the U.S., as each of the Canadian banks has some presence in the U.S. We believe banking consolidation in Canada is inevitable and we would like to be a participant.

Expansion outside North America

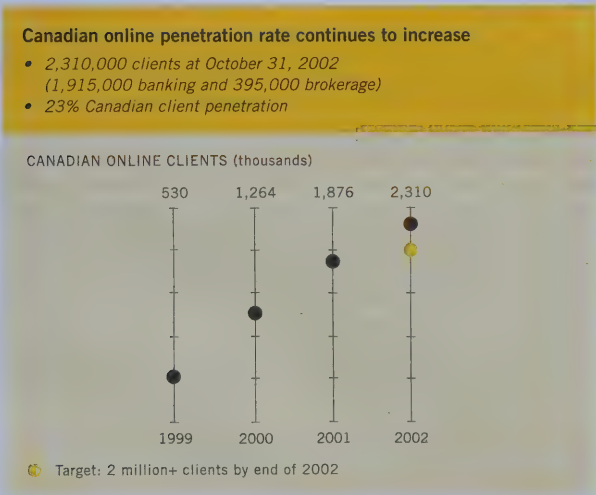
In the Caribbean, RBC Global Private Banking completed a small acquisition of clients and staff from UBS AG in the corporate servicing area with client assets of more than US\$800 million. Also, in an effort to expand our service offering to our international clients, we have expanded our brokerage offering and now have more than 60 investment advisors servicing our non-North American high net worth client base with total assets of more than \$6 billion.

RBC Capital Markets continued to build our international business, largely through the acquisition of expert teams. In 2002, the London-based structured finance team reorganized and expanded, as did the highly successful international bond business. We have also positioned ourselves structurally for future global growth with two of our five divisions now managed from outside Canada. As well, our global asset securitization business, based in New York, moved from its largely North American conduit focus to a more global framework that includes term products.

During fiscal 2002, we completed the successful integration of Australia-based Perpetual Fund Services, acquired in 2001. In addition, RBC Global Services expanded its custody business in the U.K., by signing a number of custody mandates with clients there, including J.O. Hambro and Edinburgh Fund Managers.



One of our key strategic priorities is to grow high-return or high P/E multiple businesses. While our major focus is on expanding RBC Banking and RBC Investments, each of the other business platforms has also targeted priority areas for expansion. The following pages highlight initiatives undertaken by each of our five business platforms to enhance the products and services offered to clients and the channels through which the products are delivered. These initiatives are in addition to those discussed in the North American expansion section on pages 9–12.



RBC Banking

We continued to enhance our already-strong CRM and client segmentation capabilities this year. The Direct Marketing Association Financial Services Council recognized our CRM capabilities when it named us its Company of the Year in April. We also continued to develop programs to meet the needs of specialized client segments. For example, we became the first financial institution to provide automotive dealers and independent leasing/daily rental companies with the capacity to process transactions online – at their place of business in a real-time environment. The RBC-Overdrive system, rolled out in January, also provides information pertaining to current borrowing rates, vehicle detail, interim statements and month-end reports.

We also launched a pilot of a new channel and brand to improve service to lower income urban neighbourhoods with the October opening of the Cash & Save outlet. The test site, located in the Parkdale area of Toronto, offers longer hours and quick access to a basic set of transaction services, such as cheque cashing, bill payments, wire transfers and money orders. The concept was developed in partnership with St. Christopher House, a local social services agency, and Bain & Company, a global business strategy consultancy. Further Canadian locations will be considered if the model proves sustainable.

We first introduced online banking in 1996 and have been consistently recognized by external sources as best in class. In September, we introduced a redesigned Online Banking service that offers new features and enhancements to our online banking and trading clients. We surpassed our previously established 2002 enrollment target of over 2 million clients in the second quarter of the year, and as of the end of 2002, 2.3 million clients had online access to services.

We were awarded top honours in *Investment Executive's* 2002 Account Managers' Report Card in July. The Canadian industry publication ranked Canada's major banks and credit unions by the satisfaction of their personal banking account managers.

RBC Insurance

New products focused on specialized markets and enhanced distribution capabilities characterized key initiatives taken to grow our presence in the insurance industry. Our Canadian operations expanded in 2002, with the opening of five new life insurance business development offices – in Vancouver, Regina, Mississauga, Ottawa and Halifax – and four new career sales offices located in British Columbia and Ontario.

To better support and serve the needs of Canadian life insurance professionals who sell our products, we established a new online sales resource centre in May. The Web site rbcsinsurance.com/businesspartners/life provides valuable sales tools and information to help these professionals grow their businesses. They can access current news releases, bulletins and feature articles; a knowledge centre with trade articles and presentations, product information and forms; and a sales support area that provides effective sales tools that can be sent to clients as value-added support.

Addressing a growing insurance need among Canadians who travel domestically, we introduced our Travel Within Canada program. Rolled out in February, it provides access to competitively priced comprehensive emergency medical, baggage and trip cancellation coverage for Canadians who travel within the country.

Further product development includes a critical illness insurance offering that pays out a lump sum benefit for clients who survive a wide range of specified critical illnesses, including heart attack, stroke, cancer and kidney failure. This new product, launched in November 2001, is a significant addition to our comprehensive portfolio of living benefits, complementing our industry-leading long-term care products.

Taking advantage of new distribution opportunities, RBC Liberty Insurance introduced a new term insurance product for direct consumer sales, including through the Web at rbcterminsurance.com.

RBC Investments

We enhanced our product and service offerings for Canadian clients and made moves to improve and maintain the capability of our operations in the U.S. and Latin America.

With our December 2001 launch of Fixed Income Online, clients of RBC Action Direct, our Canadian direct investing service, have been able to purchase T-bills, guaranteed investment certificates (GICs) and bonds from the largest inventory in Canada. In June, we introduced Asset Mix, an online tool to help RBC Action Direct clients calculate the appropriate asset allocation for reaching their financial objectives.

In the U.S., the strength of RBC Dain Rauscher's fixed income business was evident across the municipal and taxable arenas in 2002, particularly with Tier 2 and Tier 3 institutional investors, including depositories, investment managers, insurance companies and public funds. The fixed income business continued to achieve top 10 status in the U.S. national rankings and our national municipal rankings placed us in the top 10 in all 3 major industry measures (Lead, Co-managed and Financial Advisor). In addition, Fixed Income Capital Markets opened an RBC Products Desk in Chicago in July, providing an expanded offering of RBC Investments products for RBC Dain Rauscher's clients.

RBC Global Private Banking completed the integration of the Channel Islands trust businesses acquired from Ernst & Young in Guernsey in 1999 and Jersey in 2000, with the implementation of a common technology and single operations platform. RBC Global Private Banking also expanded its business by securing in excess of \$1.5 billion of deposits and \$2 billion of private client assets that were previously serviced by third-party banks.

RBC Capital Markets

More focused research coverage, which now extends to some 500 traded companies, and our move to centralize our U.S. equity sales and trading expertise in New York, were significant strides toward our primary objective of building a strong business among U.S. mid-market clients. Further, investment banking activities have been reinforced with a strengthened private equity capability and the consolidation of our senior mezzanine, syndication and high-yield lending activities within one origination group.

In Canada, we maintained our leading position in 2002, despite intensified competition from foreign dealers, global consolidation, currency consolidation and the steady decline in the number of top-tier Canadian firms. Our success lies in a strong relationship focus and the ability to provide clients with a full suite of investment banking services. Throughout the year, we were ranked number one or two in virtually every business according to published league tables.

We continued to build the global scope of our businesses. Our London fixed income group expanded operations through the development of a direct client e-trading system. Volumes increased substantially following the addition of the euro-denominated bonds in March, with clients able to trade electronically in over 2,000 securities in 9 currencies. Our foreign exchange business is a significant revenue producer and enjoys a world-class ranking.

Since June our newly created Alternative Investments division has responded to client needs for non-traditional opportunities to diversify their long-term investment portfolios. The unit offers clients access to private equity and hedge funds, as well as Collateralized Debt Obligations (CDO) and managed futures.

RBC Global Services

Innovations in products and services have allowed us to build upon past successes and become a leader in Canada and around the world.

We demonstrated continued leadership in providing financial services to the Canadian public sector when we launched *paytickets.ca* in January with Teranet Enterprises Inc., an innovator and leader in e-government solutions. This Web portal enables consumers to pay parking tickets and moving violations online using credit cards.

We established the infrastructure, security protocol and initial service offerings for our new Treasury Management & Trade Web platform in 2002. Our clients began accessing balance reporting and account transfers in August and, throughout 2003, they will have access to other cash management and trade services.

We successfully developed and marketed a nostro service to settle Canadian dollar transactions for Continuous Linked Settlement (CLS), our global foreign exchange settlement system. As of September, when CLS went live, we had won 50 per cent of Canadian dollar mandates for financial institutions around the world, a larger percentage than any other nostro provider of CLS services.

Our reputation for excellence in client service and product innovation led to a number of custody mandates awarded, including those by Mackenzie Financial Corporation and AIM Funds Management, Inc., representing approximately \$70 billion in assets under administration. We also expanded our outsourcing arrangement with Toronto-based CI Mutual Funds Inc., taking on responsibility for a recently acquired \$11 billion fund portfolio. We now provide services for CI's entire \$29 billion portfolio.

Major international client satisfaction surveys continued to recognize our performance. *GSCS Benchmarks* presented us with the award for best securities lending program. *Global Investor's* Global Custody Survey ranked us number one in the world for service to European clients, number one in the world for service to European institutional asset managers and number three in the world for client service quality. R&M Consultants' Global Custody Survey rated us number four in the world for client service. For the fourteenth consecutive year, we achieved top-rated status for Canadian custody services in *Global Custodian's* Agent Bank Review.

RBC Financial Group

In all of these instances, our success flowed from our strengths, including our values and employees, our client focus and our diversified business base. Our platforms' strategies and activities are guided not only by their own goals but also by RBC's overall objectives – to be the undisputed leader of integrated financial services in Canada, a best in class provider of select financial services in the U.S. and a premier provider of specialized global financial services.

As an organization, we are proud to be recognized by industry peers and observers for our innovations and strengths. Citing our successful expansion into the U.S. market and our being one of the first North American banking companies to embrace CRM, *American Banker* honoured RBC CEO Gord Nixon with the 2001 Innovator of the Year Award.

We were one of 10 organizations selected in August to be profiled in *iQ Magazine's* annual Leaders in Internet Business. The Cisco publication recognizes companies and individuals that it believes use Internet strategies to increase productivity, build client loyalty and improve efficiencies. RBC was credited for using the Web "to improve its interactions with clients, develop new lines of business and cut costs of its operations and internal processes."

We were listed in the Dow Jones Sustainability World Index for the third year in a row. DJSI World companies are chosen from 2,500 of the largest capitalized companies in the Dow Jones Global Index and recognized for leading their industries in best practices and superior environmental, social and economic performance.

We were honoured for the third year in a row and for the fifth time by *CIO Magazine* as a CIO-100 organization in its August issue. RBC was recognized for our innovative approach to meeting business objectives through the efficient and effective use of technology.

Other major citations for strategy and performance include:

- Best Financial Reporting award for Canadian public companies, *Investor Relations Magazine*, third consecutive year. Winners are chosen following feedback from Canadian portfolio managers, analysts and brokers as well as U.S. money managers and more than 500 individual investors across Canada
- Best board of directors in Canada, *Canadian Business* magazine, second consecutive year. RBC was credited for the separation of chairman and CEO offices, director independence and performance measurement, and the board's business intelligence
- Award for Excellence 2002 for best bank in Canada, *Euromoney*, on the basis of a "combination of good management and a diversified platform"
- Best bank in Canada, *Global Finance*, in their roundup of best banks in the world for 2002



We have experienced tremendous growth and change over our 133-year history, but perhaps no period has been more dramatic than the past 15 years. During this period, we expanded into new businesses, adopted new technologies and delivery channels, significantly re-aligned our operations outside Canada, and evolved new ways of doing business to meet the needs of our clients. Part of our strategy during this period consisted of organizing our business along five distinct business platforms – RBC Banking, RBC Insurance, RBC Investments, RBC Capital Markets and RBC Global Services. The first three have expanded into the U.S., and all of the platforms have been significantly restructured in the past five years.

A new strategic priority

This year we added cross-platform leverage as a fourth key priority in recognition of the fact that at an integrated financial services company such as ours, the whole has the potential to be much greater than the sum of the individual parts. In simple terms, cross-platform leverage is about working across our businesses and functions to grow revenues by sharing best practices and offering our broad array of products and solutions in an integrated fashion to our clients. It's also about cutting costs by eliminating duplication that arises when businesses and functions are run autonomously and not in an integrated fashion. Through product integration we can better serve the needs of our clients while at the same time improving client retention, revenue growth, efficiency and profitability.

Building on past success

We have been successful in cross-selling between platforms in Canada, with business referrals of \$9.3 billion between different parts of RBC generating over \$16.8 billion of new business between 1997 and 2002. That is, for every dollar of business that was referred to another part of RBC, we have garnered an additional \$1.82 of new business.

Most of the business referred to date has been from RBC Banking to RBC Investments. By referring the client to the “home of best fit,” we have improved client satisfaction and as a result been rewarded with more of their business.

We are ideally positioned to cross-sell with our complementary broad range of product and service offerings, sizeable client base, strength in CRM, established philosophy of doing what is in the best interests of the client, strong market position in Canada and a platform for growth in the U.S. We intend to intensify cross-selling initiatives in Canada and, over time, place increased importance on this initiative in the U.S. To this end, effective November 1, 2002, we introduced an updated referral initiative – RBC Referrals. Under this program, we have expanded the number of businesses and employees participating in referrals and have extended the program to include referrals between businesses pertaining to both the personal and business needs of our clients. By the end of the first quarter of 2003, all businesses across the organization should be participating in RBC Referrals. Referrals are fundamental to the way we do business, and will be integrated into all business unit strategies including those relating to sales management, performance measurement, training and development, employee recognition and client and employee satisfaction measures.

To identify potential areas for improvement in operational efficiency and growth in revenues, we have undertaken a number of initiatives in the recent past, including the E² initiative. E² stands for efficiency and effectiveness. This initiative is headed by senior management from our business platforms and functions who meet regularly to break down barriers between platforms and between businesses within platforms, eliminate duplication and identify centres of expertise that can be leveraged to enhance efficiency and revenues. To date, E² has identified over 55 projects that will result in cost savings and additional revenue. We are also currently undertaking a firm-wide review of our functions to identify areas where we can improve our agility and productivity.

RBC Banking

Perhaps the most notable example to date of two platforms collaborating in a way that leverages their respective competencies is RBC Banking and RBC Investments joining forces to deliver financial planning services through RBC Investments Financial Planning. We are well-positioned as “first-time” advice providers for clients at the beginning of their investment life cycles. However, as their investable assets grow and the complexity of their investment situation increases, they often look to independent financial planners for financial advice. This is reflected in our relatively low penetration in the Builders & Borrowers and Wealth Accumulators segments – two client segments we understand well through our CRM and market research work. The Builders & Borrowers segment comprises personal clients who are in the borrowing phase of their life cycle, whereas the Wealth Accumulator segment comprises clients whose focus is on growing investments prior to their retirement and preserving their capital. Given that an estimated \$80 to \$140 billion will transfer from one generation to the next on an annual basis in Canada for the next 50 years, we are working more proactively to develop relationships with clients in these two key segments, meet their more complex advice needs and retain them as our clients over their investment life cycle.

Under the RBC Investments Financial Planning initiative, RBC Investments is providing its expertise in compliance and investment products, whereas RBC Banking is providing the client base, sales force, business premises and sales effectiveness expertise. With over 1,600 accredited financial planners, RBC Investments Financial Planning is ideally positioned to deliver custom tailored financial planning solutions. We are in the process of implementing this initiative and have initially targeted approximately 370,000 RBC Banking high-potential clients with a focus on investment retention and wealth transfer opportunities. Approximately one-half of these clients have been contacted to ensure we are providing an appropriate level of service that suits their financial needs, with the balance expected to be contacted by the end of the first quarter of 2003. We are currently offering proprietary products and expect to introduce third-party product offerings by the end of 2003.

RBC Insurance

RBC Insurance announced the decision to add Royal Mutual Funds, RBC Advisor Funds and RBC Royal Bank GICs to its product portfolio commencing in 2003, pending regulatory approval. The addition of these products expands the range of products available to our insurance representatives to address the investment needs of our clients and provides a new and important distribution channel for RBC Funds and RBC Royal Bank GICs.

In the U.S., RBC Liberty Insurance launched the life specialist program to offer insurance solutions to RBC Centura Bank clients. Under this initiative, each mobile RBC Liberty Life Insurance specialist is assigned approximately five RBC Centura branch locations where they are designated as the life insurance professional to whom branch personnel refer qualified life insurance sales leads. This is a highly effective approach as RBC Liberty Insurance is able to leverage established banking relationships to better meet clients' life insurance needs.

RBC Investments

RBC Global Asset Management collaborated with RBC Capital Markets to develop the RBC Investments Focus List Trust to satisfy the demands of clients for a proprietary investment product whose composition and performance approximates that of the RBC Investments Focus List. Sales totalled \$321 million.

RBC Capital Markets

RBC Capital Markets and RBC Global Services worked together to develop the new RBC LinC product. This offering provides institutional investors with one-stop trade execution, clearing and custody in the Canadian market. RBC LinC simplifies the trading and settlement cycle by enabling clients to send just one set of instructions to RBC Capital Markets for settlement and clearance, with an automatic link to RBC Global Services for investment administration services.

RBC Global Services

RBC Global Private Banking, a division of RBC Investments, sourced most of its Jersey, British Isles fund administration and custody business to Institutional & Investor Services, a division of RBC Global Services. This change freed up RBC Global Private Banking resources to focus on developing new business, while at the same time leveraging Institutional & Investor Services' efficiency in the provision of investment administration services. Our clients also benefited from higher service levels.

During 2002, we were frequently asked the following questions by shareholders and analysts. Here are the answers we provided.

What credit risk management tools do you use to mitigate risk in your corporate loan portfolio?

Given the size of our balance sheet, credit risk is our largest source of risk. It is important to proactively manage our corporate loan portfolio, particularly during downturns in the economy. The goal of our credit risk management team is to evaluate and manage credit risk on an aggregate portfolio basis, and also to limit the risk associated with individual client defaults. We have been managing our loan portfolio over the past decade to lower our credit risk profile, and we have reduced our exposure as a percentage of common equity to any single company, industry or geographic area. Also, since the last economic downturn in 1991, business and government loans and acceptances have been reduced from 57 per cent of loans to 39 per cent at the end of 2002, while residential mortgages, whose loss ratios have been historically very low, have risen to 41 per cent from 27 per cent over that period.

Once credit has been extended, risk can be managed in several ways. Our portfolio is continuously managed through both periodic and event-related reviews of each borrower's risk-reward profile and borrower rating. In situations where a borrower's risk-reward profile is no longer desirable, we may use loan sales to remove the loan from our balance sheet, or we may choose not to renew the loan. We often participate in loan syndications which distribute the credit risk across a greater number of lenders. Risk is also mitigated through the use of instruments such as credit derivatives. We have purchased credit protection of approximately \$1 billion on a number of higher risk accounts.

You are generating significant capital internally. How do you plan to deploy it?

In 2002, we generated \$1.8 billion of capital internally (i.e., net income, less dividends paid on our common and preferred shares). We announced acquisitions totalling US\$610 million and paid \$764 million in connection with common share repurchases.

In deciding how to deploy our capital, we balance our need for strong capital ratios and high credit ratings against our desire to grow the business through accretive acquisitions and additional investment in our existing businesses, while enhancing returns through share repurchases and rewarding shareholders with higher dividends.

In 2003, we expect to continue to deploy our internal capital through a combination of share repurchases, reinvestment for growth, dividend payout and perhaps targeted U.S. acquisitions should they meet strategic, cultural and financial thresholds. As mentioned on page 8, our target dividend payout ratio has been raised from 30–40 per cent to 35–45 per cent.

What are you doing to maintain your strong market position in the Canadian retail banking sector?

Our Canadian personal and commercial banking business accounts for over 40 per cent of our total earnings. In Canada, we currently have

number one or number two market shares in virtually all of our retail businesses – positions we are committed to retaining. In order to maintain our leadership, we plan to enhance our client service and recently announced that we will hire 450 salespeople for our branches by early 2003 and invest \$35 million over 3 years to upgrade our branch network. In addition, our client segment strategies are designed to tailor our service offerings to meet specific segment needs, providing a differentiated experience for our clients. We will continue to manage each segment to increase client profitability and the number of products our clients hold with us.

We are also developing community banking initiatives to target underserved populations and to better serve the needs of particular communities. One such initiative, currently in a testing phase, is a new delivery channel called Cash & Save, which allows us to serve clients with their basic banking needs in a low-cost manner.

Finally, we believe that there is tremendous opportunity in the financial planning area, with RBC Banking and RBC Investments partnering to develop more proactive relationships with those clients who are looking for financial advice. Another priority is to capture a greater share of the wealth transfer between generations. The financial planning initiative will enable us to better retain and service our clients through their life cycle stages, leading to more revenue and greater client loyalty.

How are employees motivated to achieve your corporate and financial objectives?

We strongly believe that our people are vital to our success and our ability to achieve our corporate objectives. One of the key means of engaging employees is to provide reward and recognition when these goals are achieved.

We have a variety of compensation programs that reward individuals and teams for outstanding work. Employees participate in short-term performance-based incentive or commission-based programs that have a clear line of sight to our goals. By clearly connecting personal performance and corporate objectives, individual employees can see the link to our bottom line. The annual short-term bonus paid is determined by a combination of individual performance, business unit performance and performance against our overall corporate objectives. In addition, senior management and most other employees are shareholders, reinforcing the strong alignment between employee and shareholder interests.

When it comes to motivating employees to achieve top performance, given the diversity of our employees, business cultures and the markets we serve, we recognize that one size does not fit all. As a result, we have developed a Total Rewards approach that focuses on the four cornerstones of employee engagement: competitive pay, comprehensive benefit programs, opportunity for career development, and a high-performance and motivating work environment. This approach is enhancing our ability to attract, engage and retain employees as partners in our future success.

To what do you attribute the relative stability of your trading-related revenues?

We attribute our consistent performance to a number of factors, including the diversification and composition of our trading book and a conservative trading strategy that is reflected in a low Value-At-Risk and a low number of days of net trading losses. In general, our trading revenues are the result of earning competitive spreads on trading volumes rather than taking substantial proprietary positions.

Execution of this strategy provided higher revenues in equities and in the interest rate and credit-related products of the fixed income business. However, we had lower revenues in foreign exchange and money markets, due largely to lower trading volumes.

What is your economic outlook for North America for 2003?

Our economic outlook for the coming year is one of cautious optimism. A high degree of uncertainty associated with financial market turbulence, the global growth outlook and international conflict remains in place heading into 2003. That said, however, we suspect this uncertainty will gradually ebb as we move forward, paving the way for a return to stronger growth.

In Canada, tentative signs of resurgence in the corporate sector have already emerged. Job creation has been strong. Companies have increased their stock of inventories and production. Even business investment has risen, albeit modestly and unevenly, alongside a jump in profits.

Key to Canada's improving growth prospects have been a low interest rate environment and an undervalued currency. Both will continue to exert positive effects into 2003 even as they begin to reverse course with an expected increase in inflation.

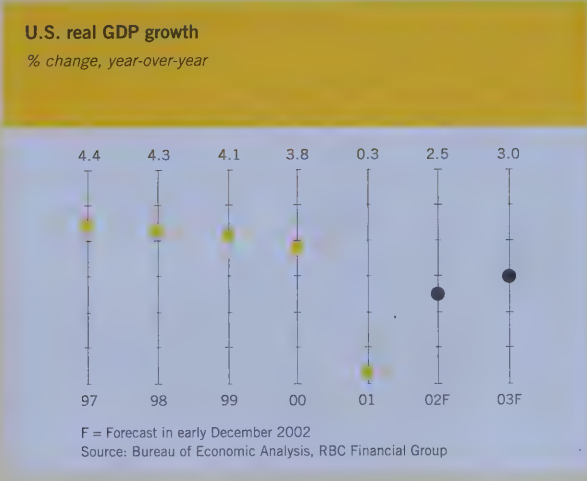
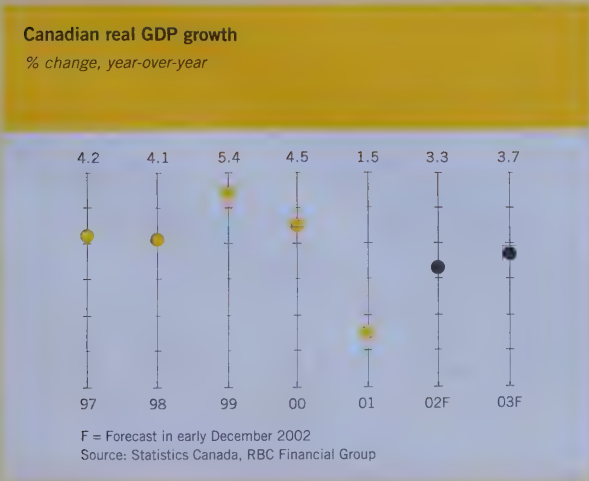
Upward price pressures, which pushed core consumer price inflation to 2.5 per cent in the fall of 2002, are likely to intensify and push core consumer inflation to the upper limit of the Bank of Canada's inflation target band of 1-3 per cent. The central bank has already responded by

hiking interest rates three times in 2002 – for a total increase of 75 basis points – only pausing late in the year as external factors put the world, and, more particularly, the U.S., economic outlook at risk.

North American prospects in 2003 depend on a turnaround in the U.S. business sector. Consumers kept the U.S. economy afloat in 2002, but will be hard-pressed to offer a repeat performance. Generational lows in interest rates induced consumers to bring forward some spending, partially satiating the appetite for durables goods, such as motor vehicles and home furnishings, in the period ahead. A low interest rate environment should prove supportive again in 2003 for consumers, but having dug into future demand, any upside to consumer spending should be limited.

Business investment and production, which began to rise earlier in 2002 alongside consumer spending, tapered off in the second half of the year as consumer, business and investor confidence sagged. Should confidence improve, however, the outlook for businesses is positive. Business inventories are low relative to sales, and profits – supported by strong productivity growth – are increasing and expected to keep increasing, although moderately, in 2003. Following a year of nearly no job growth, stalling business investment and production, 2003 should bring some welcome and much needed relief.

Notwithstanding downside risks arising from confidence, the U.S. economy is expected to expand by 3.0 per cent in 2003 after growing an anticipated 2.5 per cent in 2002. Canada's economy, being a little farther along in the growth cycle, is forecast to expand by 3.7 per cent in 2003 following an expected gain of 3.3 per cent in 2002. With business cycles slightly out of sync, the Bank of Canada may have to be somewhat more pre-emptive than the U.S. Federal Reserve at tightening monetary conditions. More interest rate hikes are expected in Canada in 2003 in a bid to keep inflation within the central bank's target band, the bulk of which are expected to come in the latter half of the year. Given the lack of inflation concerns in the U.S., we anticipate the Federal Reserve will raise rates – but by a lesser amount – starting in the fall of 2003.





In every marketplace we serve, we aspire to be known as an organization that builds enduring relationships with, and delivers value for, its clients, shareholders, employees and communities. Each of these stakeholders is important to our future. We take seriously our responsibility to offer our clients excellent service and top-quality products and access through a variety of channels, generate consistently superior long-term returns for our shareholders, provide a challenging, satisfying workplace for our employees and extend our resources to help develop vital local communities. Our values of service, teamwork, responsibility, diversity and integrity form the foundation for our commitments to our stakeholders.

Our clients

We work to build long-term relationships with every one of our 12 million clients, aiming to provide excellent value no matter what channel, product or service they use. Through market segmentation and client information expertise we are able to focus consistently on client needs, working across business platforms to develop a personalized integrated financial solution for every client. We seek to serve our clients better, to earn their loyalty and to be rewarded with more of their business. Integral to our client care commitment is prompt, efficient attention to complaints. For concerns not resolved through our established complaint management process, the Office of the Ombudsman provides an impartial appeal avenue. Further information is available at branches, online at rbc.com/ombudsman or through the office at: P.O. Box 1, Royal Bank Plaza, Toronto, Ontario, Canada, M5J 2J5. Tel: 1-800-769-2542 or 416-974-4591. Fax: 416-974-6922. E-mail: ombudsman@rbc.com.

Our shareholders

We are focused on maximizing long-term shareholder value through consistently strong financial performance and returns, disciplined and profitable international expansion, growth of high-return or high-P/E multiple businesses, and through cross-selling products and realizing cost synergies across RBC. We are committed to providing excellent service and disclosure to our shareholders and ensuring the highest standards of corporate governance. In the past five years, common shareholders have realized a 10.7 per cent compound annual total return compared to -0.3 per cent for the S&P/TSX Composite Index. We believe that the premium valuation accorded our common shares relative to other Canadian banks, in terms of price to book value and price to earnings measures, reflects the market's endorsement of our strategy, performance and outlook. Shareholder information is available at rbc.com/investorrelations.

Our employees

The strength of our people remains one of our most critical competitive advantages. Our employees' commitment to working together to meet the needs of our clients, shareholders and communities is integral to our ongoing success. RBC's values – together with a common vision, goals and strategic priorities – engage and inspire our employees as partners in shaping our future. RBC is widely recognized for its leading workplace practices, innovative continuous learning environment, career opportunities, competitive compensation and benefit programs, and commitment to valuing the diversity of its people. Approximately 85 per cent of eligible employees own our shares through our employee savings and share ownership plans.

Our community

For the last six years, *The Globe and Mail* has named us the most socially responsible corporation in Canada – a reflection of our commitment to help build healthy communities wherever we have businesses. This year, we donated more than \$37 million worldwide, including grants to after-school programs, funding for healthcare initiatives and support for community economic development. We also invested over \$20 million in amateur athletics, the arts and community events. Our employees contributed countless volunteer hours, too, sharing skills, knowledge and compassion to further enrich the communities where they live and work. But corporate citizenship should be measured not only by a company's donations, but also by its products, services and programs, the way it does business, and its leadership in key areas of social responsibility. For more information on these aspects of our corporate citizenship, visit "Community Centre" at rbc.com.

Financial review

U.S. GAAP

Caution regarding forward-looking statements

From time to time, we make written and oral forward-looking statements, included in this Annual Report, in other filings with Canadian regulators or the U.S. Securities and Exchange Commission, in reports to shareholders and in other communications, which are made pursuant to the "safe harbor" provisions of the United States *Private Securities Litigation Reform Act of 1995*. These forward-looking statements include, among others, statements with respect to our objectives for 2003, and the medium and long terms, and strategies to achieve those objectives, as well as statements with respect to our beliefs, plans, expectations, anticipations, estimates and intentions. The words "may," "could," "should," "would," "suspect," "outlook," "believe," "anticipate," "estimate," "expect," "intend," "plan," and words and expressions of similar import are intended to identify forward-looking statements.

By their very nature, forward-looking statements involve inherent risks and uncertainties, both general and specific, and risks exist that predictions, forecasts, projections and other forward-looking statements will not be achieved. We caution readers not to place undue reliance on these statements as a number of important factors could cause actual results to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements. These factors include, but are not limited to, the strength of the Canadian economy in general and the strength of the local economies within Canada in which we conduct operations; the strength of the United States economy and

the economies of other nations in which we conduct significant operations; the effects of changes in monetary and fiscal policy, including changes in interest rate policies of the Bank of Canada and the Board of Governors of the Federal Reserve System in the United States; changes in trade policy; the effects of competition in the markets in which we operate; inflation; capital market and currency market fluctuations; the timely development and introduction of new products and services in receptive markets; the impact of changes in the laws and regulations regulating financial services (including banking, insurance and securities); changes in tax laws; technological changes; our ability to complete strategic acquisitions and to integrate acquisitions; unexpected judicial or regulatory proceedings; unexpected changes in consumer spending and saving habits; the possible impact on our businesses of international conflicts and other developments including those relating to the war on terrorism; and our anticipation of and success in managing the risks implicated by the foregoing.

We caution that the foregoing list of important factors is not exhaustive. When relying on our forward-looking statements to make decisions, investors and others should carefully consider the foregoing factors and other uncertainties and potential events. We do not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on our behalf.

Management's discussion and analysis

We evaluate our performance on a reported basis (i.e., as reported in our consolidated financial statements prepared in accordance with United States generally accepted accounting principles (GAAP)) as well as on a core basis (i.e., excluding special items). We view special items as transactions that are not part of normal day-to-day business operations or are unusual in nature, thereby obscuring or distorting our analysis of trends. The special items in 2001, shown in Table 6 on page 27, total \$204 million and include gains on dispositions, a U.S. retail banking restructuring charge, income tax related to these items, and a tax expense resulting from enactments of tax rate reductions. There were no special items in 2002. Certain earnings measures, such as core earnings, do not have a standardized meaning prescribed by GAAP and therefore are unlikely to be comparable to similar measures presented by other companies. Our recent U.S. acquisitions include RBC Centura

Banks, Inc. (now includes Eagle Bancshares, Inc., RBC Mortgage and what was previously Security First Network Bank (SFNB)), RBC Liberty Insurance and RBC Dain Rauscher (includes Tucker Anthony Sutro Corporation). We present information on a core basis because some investors may also find it useful in evaluating financial performance and analyzing trends in our businesses.

The analysis and discussion that follows on pages 22 to 66 contains comparisons to 2001 that are generally based on the 2001 core numbers (i.e., excluding special items shown on page 27). The consolidated financial statements prepared in accordance with U.S. GAAP are on pages 67 to 96.

Our fiscal year-end is October 31. All dollar amounts in management's discussion and analysis are in Canadian dollars, unless otherwise specified.

Overview

| TABLE 1 Net income | | | |
|---|----------|----------|----------|
| (C\$ millions, except percentage amounts) | % change | 2002 | 2001 |
| Net income (1) | 19% | \$ 2,898 | \$ 2,435 |
| Impact of special items (2) | | — | (204) |
| Core net income | 30% | \$ 2,898 | \$ 2,231 |

(1) Net income includes goodwill amortization expense of \$250 million in 2001 (nil in 2002).
 (2) Special items are shown in Table 6 on page 27.

As shown in the tables above, full year net income increased \$463 million or 19% (16% on a per share basis). Excluding special items of \$204 million (\$.31 per share) in 2001 detailed on page 27, full year net income was up \$667 million or 30% and EPS were up 27%. Excluding special items and goodwill amortization expenses of \$250 million in 2001, net income was up \$417 million or 17% and EPS were up \$.49 or 13% in 2002 compared to 2001. This \$417 million growth was largely driven by a \$153 million increase in net income from recent U.S. acquisitions (excluding goodwill amortization expenses in 2001), cost savings of approximately \$200 million after-tax from operations other than our recent U.S. acquisitions and lower provisions for credit losses of approximately \$37 million after-tax.

On November 1, 2001, we adopted new accounting standards regarding business combinations under which goodwill is no longer amortized and is instead assessed for impairment at least annually. Accordingly, we did not incur goodwill amortization expense this year, whereas, in 2001, we incurred goodwill amortization expense of \$250 million after-tax (\$.39 per share).

Net income from our recent U.S. acquisitions was \$232 million in 2002, up from \$(80) million in 2001 (\$23) million excluding special items), partially reflecting the cessation of goodwill amortization this year, which accounted for \$102 million of the net income improvement.

| TABLE 2 Diluted earnings per share (EPS) | | | |
|--|----------|---------|---------|
| (C\$, except percentage amounts) | % change | 2002 | 2001 |
| EPS (1) | 16% | \$ 4.12 | \$ 3.55 |
| Impact of special items (2) | | — | (.31) |
| Core EPS | 27% | \$ 4.12 | \$ 3.24 |

(1) EPS includes goodwill amortization expense of \$.39 per share in 2001 (nil in 2002).
 (2) Special items are shown in Table 6 on page 27.

Excluding special items and goodwill amortization expenses, recent U.S. acquisitions resulted in an increase in net income of \$153 million, largely reflecting the acquisition of Centura Banks, Inc. on June 5, 2001, which contributed seven more months of earnings in 2002 compared to 2001, synergies achieved from the integration of Tucker Anthony Sutro (acquired on October 31, 2001) into RBC Dain Rauscher, and stronger performance from RBC Dain Rauscher's fixed income business.

The lower growth rate in EPS than in net income reflected 32 million additional average common shares outstanding in 2002 as compared to last year. This largely reflects the issuance of common shares in last year's third quarter in connection with the share exchange for the acquisition of Centura Banks, partially offset by share repurchases during 2002.

As shown in Table 3 below, in 2002, U.S. and Other International revenues were \$5.9 billion or 37% of total revenues, up from \$4.2 billion or 29% in 2001. Recent U.S. acquisitions resulted in U.S. revenues increasing to \$4.4 billion or 28% of total revenues, from \$2.9 billion or 20% in 2001.

Total U.S. net income improved to \$210 million from \$(138) million in 2001 (\$81) million excluding special items), despite higher provisions for credit losses this year, largely for the reasons described above.

| TABLE 3 Earnings by geographic segment | | | | | | | | |
|--|----------|---------------|---------------------|----------|----------|---------------|---------------------|----------|
| (C\$ millions, taxable equivalent basis) | 2002 | | | | 2001 | | | |
| | Canada | United States | Other International | Total | Canada | United States | Other International | Total |
| Net interest income | \$ 5,550 | \$ 1,262 | \$ 379 | \$ 7,191 | \$ 5,595 | \$ 485 | \$ 449 | \$ 6,529 |
| Non-interest revenue | 4,318 | 3,125 | 1,136 | 8,579 | 4,862 | 2,404 | 889 | 8,155 |
| Gross revenues | 9,868 | 4,387 | 1,515 | 15,770 | 10,457 | 2,889 | 1,338 | 14,684 |
| Provision for credit losses | 529 | 440 | 96 | 1,065 | 757 | 379 | (17) | 1,119 |
| Non-interest expense | 5,747 | 3,670 | 827 | 10,244 | 6,214 | 2,712 | 715 | 9,641 |
| Income taxes (1) | 1,442 | 67 | 54 | 1,563 | 1,529 | (64) | 24 | 1,489 |
| Net income | \$ 2,150 | \$ 210 | \$ 538 | \$ 2,898 | \$ 1,957 | \$ (138) | \$ 616 | \$ 2,435 |
| Core net income (2) | \$ 2,150 | \$ 210 | \$ 538 | \$ 2,898 | \$ 1,696 | \$ (81) | \$ 616 | \$ 2,231 |

(1) Includes non-controlling interest and taxable equivalent adjustment.

(2) Excludes special items in 2001, which are described in Table 6 on page 27. There were no special items in 2002.

Outlook

We are targeting growth in diluted earnings per share of 10–15% and a return on common equity of 17–19% in fiscal 2003 based on the expectations that our cost management efforts will allow expenses to grow at a lower rate than revenues and that capital market activity will pick up somewhat in 2003.

Financial priorities

Revenue growth and diversification

In 2002, revenues increased 7%, primarily reflecting recent U.S. acquisitions. Operating, or core, revenues (i.e., excluding special items in 2001) increased 11%, also primarily reflecting recent U.S. acquisitions, and were higher than our objective of core revenue growth of 7–10%. Excluding recent U.S. acquisitions, operating revenues were flat. Detailed discussion follows on pages 38 to 41.

Cost control

Non-interest expense increased 6% and operating non-interest expense (which excludes special items, the costs of Stock Appreciation Rights (SARs) and retention compensation associated with acquisitions) increased 8%, reflecting recent U.S. acquisitions. Operating expenses excluding recent U.S. acquisitions were down 5%. A full description is provided on pages 42 to 44.

Strong credit quality

Provisions for credit losses and nonaccrual loans declined this year despite further deterioration in the telecommunication sector. The allocated specific provision for credit losses ratio was .50% (.48% net of effect of credit derivatives) in 2002 compared to .52% in 2001, while the nonaccrual loans ratio was 1.27% versus 1.36% in 2001. During the year, net charge-offs were .71% of average loans and acceptances compared to .55% in 2001. Detailed discussion and tables are provided on pages 45 to 52.

Balance sheet and capital management

Total assets were \$382 billion at October 31, 2002, up \$19.5 billion or 5% from October 31, 2001. At October 31, 2002, using Superintendent of Financial Institutions Canada (OSFI) guidelines and Canadian GAAP financial information, our Tier 1 capital ratio was 9.3% versus 8.7% at October 31, 2001, while the Total capital ratio was 12.7% versus 11.8% at October 31, 2001. Both ratios were above our medium-term (3–5 year) capital goals of 8% for Tier 1 capital and 11–12% for Total capital. More details are provided on pages 58 to 60.

Factors that may affect future results

There are numerous factors, many beyond our control, that could cause results to differ significantly from our expectations. Some of these factors are described below. Other factors, including credit, market, liquidity, insurance, operational and other risks are described in the Risk management section beginning on page 53.

By their very nature, and as noted in the "Caution regarding forward-looking statements" on page 21, forward-looking statements involve inherent risks and uncertainties, both general and specific, and risks that predictions, forecasts, projections and other forward-looking statements will not be achieved. We caution readers not to place undue reliance on such statements in this management discussion and analysis as a number of important factors could cause actual results to differ materially from the plans, objectives, goals, targets, expectations, estimates and intentions expressed in such forward-looking statements.

Industry and non-company factors

As an integrated financial services company conducting business in Canada, the United States and other countries, our revenues and earnings are affected by the health of the economic, business and capital markets environments specific to the geographic regions in which we conduct business.

Factors such as interest rates, inflation, exchange rates, consumer spending, business investment, government spending, the health of the capital markets and terrorism impact the business and economic environment and, ultimately, the amount of business we conduct in a specific geographic region. For example, in an economic downturn characterized by higher unemployment, lower family income, lower corporate earnings, lower business investment and consumer spending, the demand for our loan and other products would be adversely affected and the provision for credit losses would likely increase, resulting in lower earnings. Similarly, a continuation or worsening of the current prolonged downturn in the equity markets could cause a further reduction in new issue and investor trading activity, assets under management (AUM) and assets under administration (AUA), resulting in lower fee, commission and other revenues.

Our earnings are affected by the monetary policies of the Bank of Canada and the Board of Governors of the Federal Reserve System in the United States.

Changes in the supply of money and the level of interest rates can impact our profitability. A decline in interest rates would result in a decrease in the net interest income earned on our non-trading portfolio and an increase in the value of our long principal positions of securities subject to interest rate risk. Conversely, an increase in interest rates would result in an increase in the net interest income earned on our non-trading portfolio and a decrease in the value of our long principal positions of securities subject to interest rate risk. For a more complete discussion of interest rate risk and its potential impact on our non-trading portfolio, please refer to the discussion of asset/liability management activities in our non-trading portfolio on page 61. For a more complete discussion of interest rate risk and its potential impact on the value of principal position of securities subject to interest rate risk, please refer to the discussion of trading activities on page 55.

Our performance can be influenced by the degree of competition in the markets in which we operate.

The competition for clients among financial services companies in the consumer and business markets in which we operate is intense. Customer loyalty and retention can be influenced by a number of factors, including relative service levels, the prices of products or services and changes in the attributes of a product or service. Customer loyalty and retention can also be compromised as a result of the client being "cross sold" by a competitor firm. Non-financial companies can provide consumers with the option to pay bills and transfer funds without involving banks. Such disintermediation could reduce fee revenues.

Changes in the statutes, regulations and regulatory policies that govern activities in our various business lines could impact our results.

Regulations are in place to protect the financial and other interests of our clients. Changes to statutes, regulations or regulatory policies, including changes in the interpretation or implementation of statutes, regulations or regulatory policies, could affect us by increasing the ability of competitors to compete with the products and services we provide. In addition, our failure to comply with applicable statutes, regulations or regulatory policies could result in sanctions and financial penalties by regulatory agencies that could adversely impact our reputation and earnings.

Although we take reasonable measures to ensure compliance with governing statutes, laws, regulations and regulatory policies in the jurisdictions in which we conduct business, there is no assurance that we will always be in compliance or deemed to be in compliance. Accordingly, it is possible that we could receive a judicial or regulatory body judgment that results in fines, damages and other costs that would have a negative impact on our earnings.

Company specific factors

Our financial performance will be influenced by our ability to execute our U.S. expansion and integration strategy.

The first phase of our U.S. expansion strategy entailed putting together the original building blocks by acquiring businesses largely in the personal and commercial banking, insurance and wealth management areas. The second phase entails building scale by adding to these original building blocks through additional strategic acquisitions, increasing revenues through greater market penetration, new product and service offerings, heightened marketing and sales initiatives and through more client referrals between the companies operating in our different business lines. The second phase also entails achieving cost synergies through the integration of the back office and head office functions of our business units. Although we regularly explore opportunities for strategic acquisitions of companies in our lines of business, there is no assurance that we will be able to continue to complete acquisitions on terms and conditions that satisfy our investment criteria. Further, although results to date have met or exceeded our targets, there is no assurance we will continue to achieve anticipated cost synergies from the integration of acquired companies. Our performance is contingent on retaining the clients and key employees of acquired companies, although there can be no assurance that we will always succeed in doing so.

Our business depends on attracting and retaining key employees.

Our success as an integrated financial services company depends to a large extent on our ability to attract and retain key employees. The competition for talented people in the financial services sector is intense. There is no assurance that we will be able to continue to attract and retain key employees, although our policies and practices are geared towards doing so and attrition at the management level is low.

Other factors

Other factors that may affect future results include changes in trade policy, the timely development and introduction of new products and services in receptive markets, changes in tax laws, technological changes, unexpected judicial or regulatory proceedings, unexpected changes in consumer spending and saving habits, the possible impact on our businesses of international conflicts and other developments including those relating to the war on terrorism, and our anticipation of and success in managing the risks implicated by the foregoing.

We caution that the foregoing discussion of factors that may affect future results is not exhaustive. When relying on forward-looking statements to make decisions with respect to Royal Bank of Canada, investors and others should carefully consider the foregoing factors, other uncertainties and potential events, and other external and company specific factors that may adversely impact future results and the market valuation placed on our common shares. We do not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by Royal Bank of Canada, or on our behalf.

Critical accounting policies

Our significant accounting policies are outlined in Note 1 on pages 72 to 75. Certain of these policies require us to make estimates or assumptions that in some cases may relate to matters that are inherently uncertain. These policies include determining the allowance for credit losses, reporting the fair value of certain financial instruments, accounting for securitizations, determining the cost and obligations associated with pensions and postretirement benefits, and valuing goodwill and other intangibles.

Allowance for credit losses

The allowance for credit losses reflects management's estimate of probable losses in our loan and off-balance sheet portfolios at the balance sheet date. We determine and maintain an allowance based on a comprehensive and systematic review of our lending and off-balance sheet portfolios. As mentioned in Note 1 on page 73, our evaluation focuses on identifying and evaluating problem accounts and estimating probable losses that may exist on the remaining portfolio.

Allocated specific allowances are maintained to absorb losses on both specifically identified borrowers and other more homogeneous loans that have been recognized as nonaccrual. The losses relating to identified large business and government debtors are estimated based on the present value of expected payments on an account-by-account basis. Management's judgment is required when forecasting the amount and timing of expected payments. The losses relating to other portfolio-type products, excluding credit cards, are based on historical net charge-off experience. This amount represents the average percentage lost on nonaccrual balances and is based on past history and management's judgment.

The allocated general allowance represents the best estimate of probable losses within the portfolio that have not been specifically identified as nonaccrual. Estimates of portfolio losses are largely dependent on portfolio quality and economic conditions. In addition to the statistical analysis performed, management's judgment is required in determining the following inputs into the models employed:

- Expected default frequency
- Loss severity
- Charge-off trends
- Economic conditions, including duration of current cycle

We determine and hold an unallocated allowance, which explicitly reflects the subjective and judgmental elements involved in our determination of credit risk and the resulting loss estimates. In determining this allowance, management considers general economic and business conditions, regulatory requirements, recent loan loss experience and trends in credit quality and concentration.

The use of different estimates or assumptions in determining the allowance for credit losses may produce significantly different provisions for credit losses and financial results.

Fair value of financial instruments

We hold financial assets and liabilities, which are carried at fair value. These financial instruments comprise assets and liabilities held in our trading portfolio, securities that are available for sale and derivative financial instruments. Fair value for a majority of financial instruments in our portfolios is determined based on quoted market prices and provides the best evidence of value since it is the result of two willing parties transacting in an open market. Note 21 on pages 95 and 96 contains disclosure regarding the estimated fair value of financial instruments.

If quoted market prices are not available for certain assets or liabilities, we use financial valuation models to determine their fair value. A provision is made in situations where we believe there is the potential the amount realized on sale will be less than the estimated fair value due to insufficient liquidity over a short period of time. We also maintain a provision for model risk, which may occur when the estimated value does not reflect the true value under certain stress market conditions. All significant financial valuation models are vetted by our risk management function, which is not involved in trading the assets and liabilities and is able to provide an independent perspective. Our internal financial valuation models for accounting are strictly controlled and regularly recalibrated, and require the approval of our risk management function. The assumptions used in the financial models are subject to management's judgment, and different assumptions may produce significantly different fair values and financial results.

As outlined in Note 1 on page 72, changes in the fair value of trading account assets and liabilities are recognized in earnings. Changes in the value of available for sale securities are recognized in other comprehensive income, which is a component of shareholders' equity. Writedowns to reflect other than temporary impairment are recognized in earnings. We regularly assess whether other than temporary impairment exists.

For derivative financial instruments, we determine fair value using various methodologies including quoted market prices, prevailing market values for similar instruments, and net present value of future cash flows and other pricing models. In determining the assumptions used in our pricing and valuation models, where appropriate, we look to external market inputs including factors such as interest rate yield curves, currency rates and price and rate volatilities for options and other derivatives. The use of methodologies, models and assumptions in pricing and valuing derivatives is subjective and requires management's judgment. The use of different methodologies, models and assumptions may result in significantly different fair values and financial results.

Securitizations

Securitization is a process by which we sell loans or other financial assets to a special purpose entity (SPE), which funds the purchase by issuing securities to investors. The return to investors is derived from the cash flows of the loans or other financial assets purchased by the SPE. Details of our securitization activities are contained in Note 7 on pages 81 and 82. A discussion of our involvements with SPEs can be found on pages 64 and 65.

The calculation of the gain or loss on our securitization transactions involves the use of estimates and assumptions including expected credit losses, payment rates, discount rates and estimated future excess spread. The use of different estimates and assumptions may produce significantly different results reported in earnings.

Pensions and postretirement benefits

We offer various pension plans and postretirement benefit plans to our employees. Note 15 on page 88 contains accounting disclosure concerning our obligations with respect to these plans. The determination of obligations under our pension and other postretirement plans and related expense requires the use of actuarial valuation methods and assumptions. Assumptions typically used in determining these amounts include, as applicable, mortality rates, rate of employee turnover, future claims costs, discount rates, future salary and benefit levels, return on plan assets and future medical costs. The fair value of plan assets is determined using market values or approximations of market values for assets where market values are not readily available. Actuarial valuations and the determination of certain market value approximations are subject to management judgment and, as a result, the prepaid benefit asset (obligation) and pension and postretirement expense may differ significantly if different assumptions are used.

Goodwill and other intangibles

As outlined in Note 4 on page 78, we adopted the Statement of Financial Accounting Standard, *Goodwill and Other Intangibles Assets* (FAS 142). Under this accounting standard, goodwill is no longer amortized but is tested at least annually for impairment at the reporting unit level. Impairment is determined by comparing the fair value of a reporting unit to its carrying value. The fair value of a reporting unit and assets and liabilities within a reporting unit may be determined using a number of market valuation methods including quoted market prices, discounted cash flows and net realizable values. Inherent in each of these valuation techniques is the use of assumptions and estimates. Both the valuation method and the assumptions and estimates used therein are based on management's judgment. The use of different judgments and estimates may produce significantly different results in applying the goodwill impairment test.

Economic Profit

In addition to using traditional measures of financial performance such as net income, EPS and return on common equity (ROE), we also evaluate our performance based on the amount of Economic Profit earned. Economic Profit measures each business segment's cash operating earnings after providing for the cost of capital committed to the segment.

Cash operating earnings is net income available to common shareholders excluding the after-tax impact of special items and amortization of goodwill and other intangibles. The equity capital charge is derived by applying the cost of common equity, which is our proxy for the after-tax return required by shareholders for the use of their capital, to the amount of average common equity, commonly referred to as Economic Capital (EC). The estimated cost of equity is reviewed annually. As the result of a decline in longer-term bond yields since the last review, the cost of common equity was reset mid-year to 11.5% from 12.5%. The average cost of common equity in 2002 was 12%.

Economic Profit does not have any standardized meaning prescribed by GAAP, and therefore the Economic Profit information that we provide is unlikely to be comparable to similar measures presented by other companies. We present information on an Economic Profit basis as it is used by our management and because some investors may also find it useful in evaluating our financial performance and analyzing trends in our businesses.

To create shareholder value from an Economic Profit point of view, one must generate cash operating earnings in excess of the common equity capital charge. Positive Economic Profit adds to shareholder value while negative Economic Profit erodes shareholder value.

Economic Profit measures the change in value created for shareholders over time, and we believe it is an effective planning tool to focus attention on shareholder value growth opportunities. In order to maximize Economic Profit, one must seek to:

- Increase cash operating earnings without tying up more capital
- Target investments in projects that yield positive economic returns
- Improve overall effectiveness of invested capital through re-allocation from less effective uses
- Improve the risk-return profiles of the lines of business

We believe that Economic Profit analysis strengthens risk management discipline, as business segments are attributed capital based on their credit, market, operational and other risks. This discipline has resulted in controlled growth and a focus on returns commensurate with risks. Furthermore, Economic Profit encourages redistribution of resources from weaker to stronger performing businesses.

As shown in Table 4 below, we had record Economic Profit of \$838 million in 2002, up from \$583 million in 2001. This increase is the result of cash operating earnings growing at a faster rate than the capital charge. The Economic Profit amounts for the business segments in 2002 and 2001 are shown in the tables on pages 28, 30, 32, 34 and 36.

TABLE 4 Economic Profit ⁽¹⁾

| (C\$ millions, except percentage amounts) | 2002 | 2001 | 2000 | 1999 | 1998 |
|---|-----------|-----------|-----------|-----------|----------|
| Net income available to common shareholders | \$ 2,800 | \$ 2,300 | \$ 2,074 | \$ 1,568 | \$ 1,627 |
| Adjustment for special items (after-tax) | — | (204) | — | 88 | 17 |
| Adjustment for amortization of goodwill and other intangibles (after-tax) | 64 | 286 | 88 | 67 | 66 |
| Cash operating earnings | 2,864 | 2,382 | 2,162 | 1,723 | 1,710 |
| Capital charge | (2,026) | (1,799) | (1,448) | (1,386) | (1,249) |
| Economic Profit ⁽¹⁾ | \$ 838 | \$ 583 | \$ 714 | \$ 337 | \$ 461 |
| Economic Profit growth | 44% | (18)% | 112% | (27)% | 23% |
| Average common equity | \$ 16,880 | \$ 13,899 | \$ 10,725 | \$ 10,268 | \$ 9,255 |
| Cost of common equity ⁽²⁾ | 12.0% | 12.9% | 13.5% | 13.5% | 13.5% |

(1) Economic Profit is cash operating earnings (i.e., net income available to common shareholders excluding the after-tax impact of special items and amortization of goodwill and other intangibles) less a charge for the cost of common equity.

(2) Average for the year.

Line of business results

Overview

Table 5 on page 27 shows our results by business segment in 2002. Our 2001 results include several special items, shown in Table 6 and described below. There were no special items in 2002.

Special items increased net income by \$204 million in 2001. There were three items that increased non-interest revenues – an \$89 million gain on the formation of the Moneris Solutions merchant card processing joint venture with Bank of Montreal, a \$43 million gain on the sale of the Group Retirement Services group pension benefits administration business and a \$313 million gain on the sale of RT Capital Management's institutional money management business. Non-interest expense increased due to a \$91 million restructuring charge related to integration and cost-saving initiatives in the U.S. retail banking platform. Income taxes were increased by a tax expense of \$101 million, reflecting a writedown of deferred tax assets due to reductions in tax rates.

We attribute common equity to our business segments based on an assessment of their credit, market, operational and other risks. Common equity in the Other segment includes equity attributed to specific functional units that are reported in Other, as well as any differences between our total common equity and common equity attributed to our businesses or our functional units. We implemented a number of changes to refine our capital attribution methodologies in early 2002, resulting in higher common equity being attributed to RBC Capital Markets and RBC Investments and lower common equity to RBC Banking and RBC Insurance compared to a year ago. However, the inclusion of a full year of operations of RBC Centura Bank in 2002, as compared to 2001, resulted in more common equity being attributed to RBC Banking. The amount of common equity attributed to the Other segment increased in 2002, largely as the result of internal capital generation outstripping the need to attribute additional common equity to the other five segments, based on an assessment of their risk profiles. Our attribution of capital to the business segments involves various assumptions and judgments.

RBC Banking produced an ROE of 19.2% and generated 53% of our net income in 2002. Net income increased 32% from 2001 and core net income (net income excluding the special items in Table 6) increased \$276 million or 22%, as discussed on page 28. This improvement partially reflected higher core earnings from U.S. acquisitions (which include RBC Centura acquired on June 5, 2001, and RBC Mortgage), which rose to \$206 million from \$21 million (\$73 million excluding goodwill amortization expense) a year ago.

RBC Insurance produced an ROE of 25.7% and generated 7% of our net income in 2002. Net income increased 10% from 2001, as discussed on page 30. RBC Liberty Insurance (acquired on November 1, 2000) contributed net income of \$23 million in 2002 compared to \$29 million (\$39 million excluding goodwill amortization expense) in 2001.

RBC Investments produced an ROE of 11.1% and generated 12% of our net income in 2002. Net income declined by 32% while core net income increased \$112 million or 48%, as discussed on page 32.

RBC Dain Rauscher (acquired on January 10, 2001) made a profit of \$3 million in 2002 compared to a loss of \$73 million (\$33) million excluding goodwill amortization) last year.

RBC Capital Markets produced an ROE of 10.5% and generated 15% of our net income in 2002. Net income increased 26% and core net income increased 17%, as discussed on page 34.

RBC Global Services produced an ROE of 28.7% and generated 6% of our net income in 2002. Net income declined by 35% while core net income declined by 8%, as discussed on page 36.

The Other segment produced an ROE of 25.0% and generated 7% of our net income in 2002. Its 2001 results are shown in Note 3 on page 77. The ineffectiveness arising from certain derivatives used as cash flow hedges, in accordance with Statement of Financial Accounting Standards, *Accounting for Derivative Instruments and Hedging Activities* (FAS 133), and gains from the securitization of mortgages contributed to the growth in earnings.

TABLE 5 Results by business segment

| (C\$ millions, taxable equivalent basis, except per share and percentage amounts) | 2002 | | | | | | | 2001 | |
|---|-------------|---------------|-----------------|---------------------|---------------------|-----------|----------|----------|----------|
| | RBC Banking | RBC Insurance | RBC Investments | RBC Capital Markets | RBC Global Services | Other (1) | Total | Core | Reported |
| Net interest income | \$ 5,576 | \$ 223 | \$ 371 | \$ 553 | \$ 136 | \$ 332 | \$ 7,191 | \$ 6,529 | \$ 6,529 |
| Non-interest revenue | 2,090 | 357 | 3,276 | 2,142 | 672 | 42 | 8,579 | 7,710 | 8,155 |
| Gross revenues | 7,666 | 580 | 3,647 | 2,695 | 808 | 374 | 15,770 | 14,239 | 14,684 |
| Provision for credit losses | 626 | — | (1) | 465 | 10 | (35) | 1,065 | 1,119 | 1,119 |
| Non-interest expense | 4,520 | 399 | 3,144 | 1,627 | 548 | 6 | 10,244 | 9,550 | 9,641 |
| Income taxes | 947 | (9) | 158 | 143 | 77 | 99 | 1,415 | 1,200 | 1,350 |
| Non-controlling interest | 8 | — | — | — | — | 100 | 108 | 107 | 107 |
| Taxable equivalent adjustment | 19 | — | — | 21 | — | — | 40 | 32 | 32 |
| Net income | \$ 1,546 | \$ 190 | \$ 346 | \$ 439 | \$ 173 | \$ 204 | \$ 2,898 | \$ 2,231 | \$ 2,435 |
| Net income | | | | | | | | | |
| As a % of total | 53% | 7% | 12% | 15% | 6% | 7% | 100% | 100% | 100% |
| % growth over prior year | 32% | 10% | (32)% | 26% | (35)% | n.m. | 19% | 1% | 10% |
| % core growth over prior year | 22% | 10% | 48% | 17% | (8)% | n.m. | 30% | | |
| Return on common equity | 19.2% | 25.7% | 11.1% | 10.5% | 28.7% | 25.0% | 16.6% | 15.1% | 16.6% |
| Economic Profit (2) | \$ 614 | \$ 100 | \$ (14) | \$ (55) | \$ 100 | \$ 93 | \$ 838 | \$ 583 | \$ 583 |
| Diluted EPS | | | | | | | \$ 4.12 | \$ 3.24 | \$ 3.55 |

(1) Represents other activities, which mainly comprise Corporate Treasury, Corporate Resources, Systems & Technology and Real Estate Operations.

(2) Economic Profit is cash operating earnings (i.e., net income available to common shareholders excluding the after-tax impact of special items and amortization of goodwill and other intangibles) less a charge for the cost of common equity.

n.m. not meaningful

TABLE 6 Special items affecting business segment results in 2001 (1)

| (C\$ millions, taxable equivalent basis, except per share amounts) | RBC Banking | RBC Insurance | RBC Investments | RBC Capital Markets | RBC Global Services | Other (2) | Total |
|--|-------------|---------------|-----------------|---------------------|---------------------|-----------|--------|
| Non-interest revenue | | | | | | | |
| Gain on formation of Moneris Solutions joint venture | \$ — | \$ — | \$ — | \$ — | \$ 89 | \$ — | \$ 89 |
| Gain on sale of Group Retirement Services | 7 | — | 36 | — | — | — | 43 |
| Gain on sale of RT Capital Management | — | — | 313 | — | — | — | 313 |
| | 7 | — | 349 | — | 89 | — | 445 |
| Non-interest expense | | | | | | | |
| U.S. retail banking restructuring charge | 91 | — | — | — | — | — | 91 |
| Total impact (pre-tax) | (84) | — | 349 | — | 89 | — | 354 |
| Income taxes | | | | | | | |
| On items listed above | (33) | — | 70 | — | 12 | — | 49 |
| Enactment of change in tax rates | 45 | — | 5 | 27 | — | 24 | 101 |
| Total impact (after-tax) | \$ (96) | \$ — | \$ 274 | \$ (27) | \$ 77 | \$ (24) | \$ 204 |
| Impact on diluted EPS | | | | | | | \$.31 |

(1) There were no special items in the RBC Insurance segment in 2001. No special items at all in 2002.

(2) Represents other activities, which mainly comprise Corporate Treasury, Corporate Resources, Systems & Technology and Real Estate Operations.

RBC Banking

Business profile

RBC Banking serves over 11 million individuals, small and medium-sized businesses, and mid-market commercial clients in Canada, the U.S., the Caribbean and the Bahamas. Our distribution capabilities include a network of branches, business banking centres and other sales units, accredited financial planners, mobile sales representatives, automated banking machines, and telephone and Internet banking channels. We deliver a wide range of financial services including deposit accounts, investments and mutual funds, financial planning and advice, credit and debit cards, business and personal loans, and residential and commercial mortgages.

Industry profile

In Canada, personal and commercial banking is a mature industry dominated by the five largest Canadian banks, although competition is fierce and niche players are increasing their presence in select businesses such as credit cards. The U.S. market is more fragmented, although many regional markets are highly competitive. Many banks have expanded their focus to include offering investment products and financial advice and planning to affluent and other targeted clients. Critical success factors, in our opinion, include providing a differentiated client experience and maintaining rigorous credit and operational risk management practices and expense control.

Our strengths

- Customer relationship management (CRM) combined with strong client contact capabilities and specialized sales forces
- Established Canadian retail banking brand
- Comprehensive product, service and physical and alternative distribution capabilities compared to niche players
- Highest client household penetration ratio in personal segments, and lead product market share in business markets among Canadian banks
- Among the strongest efficiency ratios of the Big 5 Canadian banks
- Acquisition integration capabilities in the U.S. market

Our strategy

Our vision is to grow profitable relationships with each one of our business and personal clients by creating a tailored client experience for our clients across North America, while reducing costs, and effectively managing risk and capital.

We plan to achieve our vision through the following strategic priorities:

- Ensure strong revenue growth in Canada by maximizing client retention, deepening client relationships, capturing intergenerational wealth transfer opportunities and building on our financial planning and advice capabilities
- Create a differentiated customer experience, providing a valued and superior level of service tailored to customer segment needs that builds customer loyalty and clearly differentiates us from the competition
- Accelerate U.S. revenue and earnings growth by expanding our footprint in the southeastern U.S. and building a scalable platform
- Reinforce cost management and risk mitigation through effective use of technology, strengthened low cost delivery capabilities, and rigorous management of credit, operational, regulatory and compliance risk
- Cross-platform leverage by increasing referrals and cost efficiencies across RBC in Canada and the U.S.

Outlook for 2003

Based on our expectation of rising interest rates in Canada in 2003, we anticipate that the spread compression on deposits will ease. This, combined with reasonable loan growth, should have positive implications for revenue growth in our Canadian business. In the U.S., we anticipate branch openings and the acquisitions of Eagle Bancshares in July 2002 and of Admiralty Bancorp, Inc. (expected to close in January 2003) to have a positive impact on revenues. We also expect that the realization of a full year of cost synergies from the Eagle Bancshares acquisition will contribute to net income growth at RBC Centura. Overall, we expect solid earnings growth for this segment based on our continued focus on cost containment and credit and operational risk management and the benefits of a recovering economy.

Financial performance

Net income was up 32% from last year while core net income was up \$276 million or 22%. Earnings from the segment's U.S. acquisitions rose to \$206 million in 2002 from \$(36) million last year or \$21 million excluding costs related to U.S. retail bank restructuring in 2001 (\$73 million further excluding goodwill amortization expense in 2001). The higher U.S. earnings reflected the acquisition of Centura Banks on June 5, 2001, integration cost savings and revenue growth. Core net income excluding U.S. acquisitions grew 7% due to continued cost management initiatives. Core ROE increased to 19.2% in 2002 from 18.3% despite higher average common equity attributed to this segment due to U.S. acquisitions and additional business activity.

Revenues increased \$444 million or 6% from 2001, reflecting the contribution of RBC Centura (including RBC Mortgage) and the acquisition of Eagle Bancshares, which was completed on July 22, 2002. Revenues from U.S. acquisitions increased \$635 million in 2002, without which the segment's revenues would have decreased 3% due to narrower net interest margins and lower lending volumes.

Non-interest expense increased \$132 million or 3% from last year, while the efficiency ratio declined 180 basis points, as revenues grew faster than expenses. Core non-interest expense (which excludes \$91 million of costs related to U.S. retail bank restructuring in 2001) increased \$223 million or 5%. U.S. acquisitions contributed \$330 million of the core expense growth. Excluding U.S. acquisitions, core expenses fell 3%, reflecting ongoing cost management.

The total provision for credit losses fell 14% from last year, largely in the commercial loan portfolio. Nonaccrual loans decreased by \$144 million or 11%, reflecting improvements in both the Canadian consumer and Canadian commercial loan portfolios.

Results

| (C\$ millions, taxable equivalent basis, except percentage amounts) | % change | 2002 | 2001 |
|---|----------|------------|------------|
| Net interest income | 4% | \$ 5,576 | \$ 5,349 |
| Non-interest revenue | 12 | 2,090 | 1,873 |
| Gross revenues | 6 | 7,666 | 7,222 |
| Provision for credit losses | | | |
| Allocated specific | (5) | 626 | 662 |
| Allocated general and unallocated | n.m. | — | 70 |
| Total | (14) | 626 | 732 |
| Non-interest expense (1) | 3 | 4,520 | 4,388 |
| Net income before income taxes | 20 | 2,520 | 2,102 |
| Income taxes | 4 | 947 | 912 |
| Non-controlling interest | (20) | 8 | 10 |
| Taxable equivalent adjustment | 217 | 19 | 6 |
| Net income | 32 | \$ 1,546 | \$ 1,174 |
| U.S. net income | n.m. | \$ 206 | \$ (36) |
| Net income as a % of total bank net income | 500 bp | 53% | 48% |
| ROE | 240 bp | 19.2% | 16.8% |
| Economic Profit | 47% | \$ 614 | \$ 419 |
| Net interest margin | (18)bp | 3.56% | 3.74% |
| Efficiency ratio | (180)bp | 59.0% | 60.8% |
| Operating efficiency ratio (2) | (70)bp | 58.8% | 59.5% |
| Average assets | 9% | \$ 156,500 | \$ 143,000 |
| Average loans and acceptances | 7 | 144,400 | 135,400 |
| Average deposits | 10 | 122,900 | 111,400 |
| Average common equity | 16 | 7,800 | 6,700 |
| Core results (3) | | | |
| Gross revenues | 6 | 7,666 | 7,215 |
| Non-interest expense | 5 | 4,520 | 4,297 |
| Net income | 22 | 1,546 | 1,270 |
| U.S. net income | 881 | 206 | 21 |
| ROE | 90 bp | 19.2% | 18.3% |
| Credit information | | | |
| Nonaccrual loans | (11)% | \$ 1,157 | \$ 1,301 |
| Net charge-offs | 3 | 744 | 724 |
| Net charge-offs as a % of average loans and acceptances | (1)bp | .52% | .53% |
| Number of employees (full-time equivalent) | — | 35,014 | 34,845 |

(1) Includes goodwill amortization expense of \$54 million in 2001 (nil in 2002).

(2) Efficiency and operating efficiency ratios are defined on page 104.

(3) Excluding special items in 2001 detailed in Table 6 on page 27. Only the lines affected by special items are shown here.

n.m. not meaningful

Strategy by division

Canada

Operating in Canada under the RBC Royal Bank brand, we serve individuals, small and medium-sized businesses, and commercial clients in all provinces and territories. We offer our clients extensive physical and alternative distribution choices. We continue to strengthen our channel distribution capabilities, including significant reinvestment in our branch network and staff, and in our electronic banking capabilities.

We offer a wide range of financial services and advice, as detailed in our business profile on page 28, and products and expertise in specialized areas such as foreign exchange and venture capital financing. We also provide individual and business clients with a full choice of Visa credit card products, debit cards and other smart card applications. We provide merchants with credit and debit card acceptance services, point-of-sale capabilities and Internet-secure electronic transaction solutions through Moneris Solutions, a joint venture in which we participate equally with Bank of Montreal, managed through RBC Global Services.

Our goal is to grow profitable relationships with each one of our business and personal clients, using our expertise in customer relationship management, sales management and client segmentation. We will drive revenue growth by creating a tailored client experience, leveraging client life events and providing financial planning and advice to broaden client relationships using the full capabilities of RBC.

We will continue to reinforce our cost management focus by leveraging e-enabled technology and cross-platform economies of scale. We will continue to rigorously focus on the management of credit, operational and compliance risk, including fraud management initiatives and strengthened credit-scoring capabilities.

United States

RBC Centura serves as the focal point of our personal and commercial banking businesses in the U.S. Headquartered in Rocky Mount, North Carolina, RBC Centura serves individual and business clients in the southeastern U.S. RBC Centura also includes RBC Mortgage, a Chicago-based national retail mortgage originator, and RBC Builder Finance, a Houston-based financing division for home builders and developers. RBC Centura's footprint expanded in 2002 with the acquisition of Eagle Bancshares, which operated 14 branches in the Atlanta, Georgia metropolitan area. RBC Centura has also announced a definitive merger agreement with Admiralty Bancorp, which currently operates 10 branches in Florida, expected to close in January 2003.

Our U.S. priorities include:

- Expanding in the southeastern U.S. through targeted acquisitions and a build/buy branch expansion strategy
- Rapidly building a scalable platform to support growth
- Accelerating introduction of sales and marketing initiatives
- Growing national niche lines of business such as builder finance and residential mortgages
- Realizing synergies from functional integration and cross-selling opportunities across RBC's entire platform

Caribbean and the Bahamas

Operating under the brand name RBC Royal Bank of Canada, we provide a broad range of personal and commercial banking products and services to individual and business clients in the Bahamas, Barbados, the Cayman Islands and Eastern Caribbean Islands through a network of branches and automated banking machines.

Financial highlights by division

Revenues from the domestic business decreased \$201 million or 3% from 2001, primarily due to continued spread compression on core deposits and lower personal and business lending volumes. These decreases more than offset higher residential mortgage and deposit balances and wider net interest margin earned on mortgages and credit cards. Mortgage balances increased as the low interest rate environment encouraged home purchases. Deposit balances grew while lending volumes declined, reflecting consumer and business uncertainty regarding the economy and capital markets.

Results

| (C\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|--|----------|-----------|-----------|
| Gross revenues | (3)% | \$ 6,109 | \$ 6,310 |
| Average residential mortgages | 5 | 68,200 | 64,800 |
| Average personal loans | (4) | 23,600 | 24,500 |
| Average personal deposits | 2 | 74,400 | 72,900 |
| Average business loans and acceptances | (5) | 34,100 | 36,000 |
| Average business deposits | 9 | 30,500 | 28,100 |
| Average card balances | 3 | 6,200 | 6,000 |
| Card spending volumes | 2 | 26,700 | 26,300 |
| Number of: | | | |
| Employees (full-time equivalent) | 1 | 29,716 | 29,554 |
| Automated banking machines | (2) | 4,151 | 4,236 |
| Branches | (1) | 1,117 | 1,125 |
| Online clients | 23 | 2,311,915 | 1,876,358 |

Revenues increased \$635 million due mainly to a full year of RBC Centura results in 2002 compared to 5 months in 2001, as well as the contribution of Eagle Bancshares since July 22, 2002. Growth in average balances also largely reflects the inclusion of a full year of RBC Centura. Strong growth in mortgage originations and volumes at RBC Mortgage reflected high refinance activity resulting from the favourable interest rate environment.

Results

| (C\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|--|----------|----------|--------|
| Gross revenues | 94% | \$ 1,314 | \$ 679 |
| Average residential mortgages | 81 | 2,900 | 1,600 |
| Average personal loans | 154 | 3,300 | 1,300 |
| Average personal deposits | 121 | 8,600 | 3,900 |
| Average business loans and acceptances | 126 | 8,800 | 3,900 |
| Average business deposits | 93 | 5,400 | 2,800 |
| Average card balances | - | 100 | 100 |
| Card spending volumes | 100 | 400 | 200 |
| Mortgage originations (\$ billions) | 50 | 33.7 | 22.5 |
| Number of: | | | |
| Employees (full-time equivalent) | 1 | 4,181 | 4,126 |
| Automated banking machines | 7 | 275 | 258 |
| Branches (1) | 1 | 245 | 242 |
| Online clients | 18 | 89,434 | 75,887 |

(1) Excludes RBC Mortgage and RBC Builder Finance sales offices of 252 in 2002 and 264 in 2001.

Revenues increased \$10 million or 4% from 2001, aided by the sale of property in the Cayman Islands, which accounted for approximately half of the increase.

Results

| (C\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|--|----------|--------|--------|
| Gross revenues | 4% | \$ 243 | \$ 233 |
| Number of: | | | |
| Employees (full-time equivalent) | (4) | 1,117 | 1,165 |
| Automated banking machines | 11 | 60 | 54 |
| Branches | 10 | 43 | 39 |

RBC Insurance

Business profile

Operating as RBC Insurance, we provide a wide range of creditor, life, health, travel, home, auto and reinsurance products and services to more than five million clients in Canada, the U.S. and internationally. These products and services are offered through a wide variety of distribution channels, including the telephone, independent brokers, travel agents, a proprietary sales force and the Internet.

Industry profile

The Canadian insurance industry generates almost \$60 billion in premiums annually from more than 100 life insurance companies and more than 200 property and casualty insurers. Our U.S. business is focused in the life insurance sector, which is both competitive and fragmented and includes over 1,200 national and regional companies. The international reinsurance industry is dominated by several global players but also includes a number of niche companies.

Across all of our business lines, we are seeing a number of key trends, including consolidation, increased government regulation, shifting distribution opportunities, the convergence of insurance and investment products and increased globalization.

Our strengths

- A diverse set of products designed to meet a wide range of consumer needs
- Multiple distribution channels, which are supported by strong infrastructure and sales expertise
- A strong brand. As part of RBC Financial Group, we have access to a broad range of financial services, distribution channels and client base
- Market leadership in a number of Canadian insurance markets, including travel and individual life insurance

Our strategy

We are focused on growing our insurance organization by offering a wide range of products and services through multiple distribution channels in Canada, as well as in select U.S. and international markets. To accomplish this we will seek to:

- Ensure as many RBC clients as possible have an insurance relationship with RBC Insurance
- Target reinsurance activities that support and enhance the overall profitability of the insurance operations
- Continue to expand in the U.S. by utilizing existing scale and expanding the platform, entering new markets and focusing on cross-platform initiatives across RBC
- Build an integrated North American insurance platform by leveraging cross-border synergies where permitted, including the implementation of common administrative and technology systems

Outlook for 2003

Our expectation of reasonable economic growth in both Canada and the U.S. should have a favourable impact on the insurance business in 2003. Our outlook is for strong revenue growth across our operations, driven by expansion into new markets as discussed in our strategy, and the pending acquisition of the U.S. life insurance operation of Business Men's Assurance Company of America (BMA). The acquisition of BMA is subject to regulatory approvals and other customary closing conditions. We anticipate that cost reductions from the realization of cross-border synergies will also help to drive net income growth.

Financial performance

Net income increased 10% from last year and, excluding goodwill amortization expenses in 2001, was up 1%. Earnings in 2001 were adversely affected by claims resulting from the World Trade Center tragedy. RBC Liberty Insurance contributed \$23 million to net income in 2002, down from \$29 million (\$39 million excluding goodwill amortization) last year. The decline in RBC Liberty Insurance earnings was largely related to higher policy surrenders and lower earnings at its outsourcing divisions. Excluding RBC Liberty Insurance, net income increased 16%, largely reflecting strong growth in the Canadian and reinsurance businesses.

ROE improved to 25.7% from 20.0% in 2001, reflecting higher net income, as well as lower average common equity, which reflected a revised methodology for attributing capital to our insurance operations.

Premiums & deposits were up 12% from last year and revenues were up 7%, due largely to higher revenues from RBC Liberty Insurance. RBC Liberty Insurance reported 13 months of results in 2002 versus 11 months in 2001, as its reporting period was changed from September 30 to October 31 to be consistent with our fiscal year. Excluding these additional months of RBC Liberty Insurance, premiums & deposits grew 8% and revenues were flat.

Expenses grew \$24 million or 6%, largely due to the two additional months of RBC Liberty Insurance and an increase in the number of employees, partly offset by the cessation of goodwill amortization this year. Excluding the additional months of RBC Liberty Insurance, expenses fell 2%.

Results

| (C\$ millions, except percentage amounts) | % change | 2002 | 2001 |
|--|----------|----------|----------|
| Premiums & deposits | 12% | \$ 2,023 | \$ 1,812 |
| Non-interest revenue | | | |
| Earned premium | 10 | 1,564 | 1,419 |
| Fee revenue/Other | 38 | 179 | 130 |
| Less: Policy benefits | 10 | 1,081 | 985 |
| Less: Acquisition costs | 34 | 305 | 228 |
| | 6 | 357 | 336 |
| Net interest income | 8 | 223 | 206 |
| Gross revenues | 7 | 580 | 542 |
| Non-interest expense (1) | 6 | 399 | 375 |
| Net income before income taxes | 8 | 181 | 167 |
| Income taxes | n.m. | (9) | (6) |
| Net income | 10% | \$ 190 | \$ 173 |
| U.S. net income | (10) | \$ 35 | \$ 39 |
| Net income as a % of total bank net income | — | 7% | 7% |
| ROE | 570 bp | 25.7% | 20.0% |
| Economic Profit | 39% | \$ 100 | \$ 72 |
| Average assets | 10 | 6,900 | 6,300 |
| Average common equity | (12) | 700 | 800 |
| Number of employees (full-time equivalent) | 2% | 2,641 | 2,583 |

(1) Includes goodwill amortization expense of \$15 million in 2001 (nil in 2002).

Strategy by division

Life

Our life business provides a wide range of individual and group life and health insurance products to both individual and business clients in Canada and the U.S., as well as life reinsurance and retrocession to businesses around the world.

In Canada, life and health insurance products are distributed through a network of more than 7,000 independent brokers, over 550 proprietary insurance representatives and a direct sales unit. In the U.S., Greenville, South Carolina-based Liberty Life Insurance Company provides life and health insurance products through a proprietary sales force of over 600 agents and also offers select products through direct channels.

Our goal is to continue to grow our life businesses by expanding our client base and range of products and services offered, as well as by enhancing our distribution networks.

Non-life

Our non-life business includes home, auto, travel and property reinsurance for individual and business clients in Canada and select international markets.

We provide Canadians with a wide range of auto and home insurance products, offering them to individual clients and employee and affinity groups through direct sales and face-to-face channels. Travel products, which are sold through travel agents, the Internet and bank channels in Canada, include trip cancellation insurance, out-of-country medical and baggage insurance.

We participate in the property reinsurance business by accepting a share of the risk on property policies issued by other insurance companies. The majority of our current business is generated from insurance companies in the U.S. and Europe.

Our goal is to grow our non-life business by continuing to build our domestic home and auto business, entering new travel insurance markets and effectively managing our property reinsurance portfolio.

Fee businesses

We are involved in a number of other key insurance and related activities that generate fee income, including travel assistance services, structured reinsurance, the administration of bank creditor insurance programs and a proprietary sales distribution network.

Our travel and emergency assistance services include co-ordinating the delivery of emergency health, evacuation and transportation services when clients have a travel emergency, while our structured reinsurance business provides solutions to help corporations better manage financial risk.

In the U.S., our fee businesses include outsourcing services and administration and software systems provided through Liberty Insurance Services Corporation (LIS). The Business Process Outsourcing division of LIS provides services such as underwriting, billing and collection, and claims processing for nearly 4 million policies under administration. The Software Solutions division develops Web-enabled software for life, health, annuity and reinsurance administration. Together, these divisions have more than 200 client sites and serve domestic, international and multinational insurers worldwide.

Our goal is to continue to leverage our existing infrastructure and technology to enhance existing programs and grow these businesses.

Financial highlights by division

Premiums & deposits for the life business increased 10% in 2002, partially due to 2 additional months of RBC Liberty Insurance as it reported 13 months of results in 2002 versus 11 months in 2001. Without these additional months, premiums & deposits would have been up 5%, reflecting the continued strength of both the Canadian and reinsurance businesses. Lower investment income due to the low interest rate environment, as well as higher policy surrenders at RBC Liberty Insurance, contributed to the 5% decline in revenues.

Results

| (C\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|----------|----------|
| Premiums & deposits | 10% | \$ 1,529 | \$ 1,393 |
| Gross revenues | (5) | 429 | 450 |
| Average assets | 8 | 5,700 | 5,300 |
| Number of: | | | |
| Life and health policies in force in Canada (thousands) | 11 | 2,930 | 2,645 |
| Life policies in force in the U.S. (thousands) | (11) | 2,325 | 2,600 |
| Assets under management in the U.S. | (2) | 367 | 375 |
| U.S. sales agents | (4) | 690 | 718 |

Revenues from our non-life business were higher in 2002 due to stronger performance in our property reinsurance and travel businesses as last year's revenues were adversely affected by claims resulting from the World Trade Center tragedy.

Results

| (C\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|--|----------|--------|--------|
| Premiums & deposits | 14% | \$ 413 | \$ 363 |
| Gross revenues | 88 | 47 | 25 |
| Average assets | — | 700 | 700 |
| Number of: | | | |
| Home and auto – personal lines policies in force (thousands) | 37 | 93 | 68 |
| Travel – coverages (thousands) | (7) | 2,339 | 2,510 |

The substantial growth in premiums & deposits was attributable to structured reinsurance premium increases, which offset slower growth at our outsourcing divisions in the U.S. The increase in revenues reflected the stronger performance in structured reinsurance and the reporting of two additional months of RBC Liberty Insurance. Our career sales force grew substantially in 2002, reflecting increased investment in our proprietary sales distribution network.

Results

| (C\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|-------|-------|
| Premiums & deposits | 45% | \$ 81 | \$ 56 |
| Gross revenues | 55 | 104 | 67 |
| Average assets | 67 | 500 | 300 |
| Number of: | | | |
| Career sales – agents | 22 | 554 | 455 |
| Assistance services – calls (thousands) | (3) | 681 | 699 |
| Policies under administration in the U.S. (thousands) | (6) | 4,100 | 4,342 |

RBC Investments

Business profile

RBC Investments provides full-service and self-directed brokerage, financial planning, investment counselling, personal trust, private banking and investment management products and services primarily to private clients in Canada, the U.S. and internationally. Products and services are delivered through the RBC Royal Bank branch network across Canada, RBC Investments offices, RBC Dain Rauscher branches in the U.S., private banking offices and other locations worldwide. Services are also delivered via the Internet and telephone. In September 2002, we realigned parts of our Canadian distribution channels under a single management structure to enhance the client experience by offering seamless, comprehensive solutions.

Industry profile

Wealth management is a highly competitive business with numerous large and boutique firms serving the affluent and high net worth client. Many of these firms have recently developed strategies focused on attracting the high net worth market. Volatile markets and the rising costs of managing the risks inherent in the business are changing the approach and profitability of some of the players. Consolidation in the mutual fund industry has not significantly altered the competitive landscape as distribution channels continue to be expanded by all players. Self-directed brokerage businesses have come under increased pressure due to reduced transaction volumes in light of market conditions, and clients using non-revenue generating services such as research, quotes and online asset mix calculators.

Our strengths

- Relationship management capabilities from experienced people and technology applications
- Ability to deliver the choice of products and services clients need to meet their financial goals
- Multiple distribution channels for client convenience
- Ability to access entire RBC client base
- Solutions designed for specific investment strategies and client risk tolerance

Our strategy

Our goal is to be a leading provider of personalized, comprehensive investment solutions for private clients worldwide, aligning them with client needs and the markets where we serve them.

In Canada:

- Match distribution channel and type of service to client needs and preferences
- Seek lifelong and intergenerational relationships with clients by offering products and services for each stage of their wealth management needs

In the United States:

- Grow through broadening and deepening relationships with existing clients as well as through targeted acquisitions over time in order to generate greater market share and scale

Internationally:

- Provide specialized global services to clients located around the world
- Offer solutions and provide advice and choice in an increasingly transparent international business

Outlook for 2003

Based on our expectation that investor confidence and capital markets performance will begin improving only by the third quarter of 2003, we expect moderate revenue growth in 2003. Cost containment efforts should help to keep the rate of expense growth below that of revenue growth. Retention compensation costs relating to recent U.S. acquisitions are forecast to be approximately \$40 million lower in 2003, further contributing to net income growth.

Financial performance

Net income was down 32% while core net income was up 48%. The growth in core net income was due to higher earnings from RBC Dain Rauscher, as well as the cessation of goodwill amortization this year (goodwill amortization was \$110 million in 2001). RBC Dain Rauscher's net income was \$3 million in 2002, compared to a loss of \$73 million last year (\$33 million loss excluding goodwill amortization). The improvement in RBC Dain Rauscher's net income occurred despite higher retention compensation costs and reflected the acquisition of Tucker Anthony Sutro on October 31, 2001 (since integrated into RBC Dain Rauscher) and strong performance from its fixed income division. Excluding RBC Dain Rauscher, core net income would have grown 12%, largely due to the cessation of goodwill amortization in 2002. ROE was largely unchanged from last year, excluding the gain on the sale of RT Capital Management.

Revenues were up 12% from 2001, or 26% excluding special items in 2001. Revenue growth reflected the acquisition of Tucker Anthony Sutro and strong results from the fixed income division of RBC Dain Rauscher. Excluding RBC Dain Rauscher's revenue growth of \$875 million, core revenues were down 6% due to weak client trading volumes in 2002.

Expenses increased 25% over a year ago, reflecting the acquisition of Tucker Anthony Sutro and higher retention compensation related to U.S. acquisitions, which increased to \$107 million from \$88 million in 2001, with \$45 million attributable to Tucker Anthony Sutro. RBC Dain Rauscher contributed \$774 million of the expense growth in 2002. Excluding RBC Dain Rauscher, expenses fell 9%, reflecting the cessation of goodwill amortization this year, higher expenses in 2001 from a \$38 million writedown of goodwill relating to Connor Clark, and good expense management.

Results

| (C\$ millions, except percentage amounts) | % change | 2002 | 2001 |
|--|-----------|---------|---------|
| Net interest income | (3)% | \$ 371 | \$ 384 |
| Non-interest revenue | 15 | 3,276 | 2,859 |
| Gross revenues | 12 | 3,647 | 3,243 |
| Provision for credit losses | | | |
| Allocated specific | (150) | (1) | 2 |
| Total | (150) | (1) | 2 |
| Non-interest expense (1) | 25 | 3,144 | 2,510 |
| Net income before income taxes | (31) | 504 | 731 |
| Income taxes | (29) | 158 | 223 |
| Net income | (32)% | \$ 346 | \$ 508 |
| U.S. net income | n.m. | \$ (1) | \$ (81) |
| Net income as a % of total bank net income | (900)bp | 12% | 21% |
| ROE | (1,590)bp | 11.1% | 27.0% |
| Economic Profit | (114)% | \$ (14) | \$ 97 |
| Average common equity | 67 | 3,000 | 1,800 |
| Core results (2) | | | |
| Gross revenues | 26 | 3,647 | 2,894 |
| Net income | 48 | 346 | 234 |
| ROE | (80)bp | 11.1% | 11.9% |
| Number of employees (full-time equivalent) | 14% | 12,001 | 10,512 |

(1) Includes goodwill amortization expense of \$110 million in 2001 (nil in 2002).
(2) Excluding special items in 2001 detailed in Table 6 on page 27. Only the lines affected by special items are shown here.
n.m. not meaningful

Strategy by division

Canada

Financial Planning

The new financial planning platform is operated jointly with RBC Banking. This group serves branch-based clients typically with more than \$50,000 in investable assets of which a portion must include mutual funds or managed assets. Financial planning has 1,100 relationship financial planners and 550 commission-based investment and retirement planners who are also financial planners and licensed mutual fund salespeople.

Canadian & International Brokerage group

This group includes our private client division (full-service brokerage) and RBC Action Direct (self-directed brokerage) and serves both investors requiring advisor-based comprehensive financial solutions and self-managed investors. Services are provided by over 1,420 investment advisors, over 180 investment representatives, as well as via telephone and the Internet. This group also includes the International Advisory Group, which has both Canadian and internationally-based employees serving international clients. Our goal is to maintain our market position in Canada by continuing to build and enhance existing client relationships.

RBC Global Private Banking (Canada)

Our private counsel, personal trust and private banking groups serve high net worth clients across Canada, and offer a relationship management approach for the client in need of sophisticated solutions. This group works with RBC Global Private Banking (international) to ensure we can serve clients who have interests in Canada as well as around the world. In Canada, 60 investment counsellors, 80 trust officers and 200 private bankers are in locations across the country.

Global Asset Management

This unit includes RBC Global Investment Management and RBC Funds, Canada's second largest mutual fund company. We directly manage more than \$40 billion of assets in mutual and pooled funds as well as other client assets. We provide proprietary and externally-managed investment management products and advisory services through RBC Royal Bank, RBC Investments' distribution businesses and external distributors to private and institutional clients in Canada and worldwide. Our family of mutual funds and other pooled products encompass a broad range of investment solutions including money market, fixed income, balanced and Canadian, U.S. and global equity funds, as well as alternative investments. In 2003, our goal is to continue the strategy, first implemented in 2001, to broaden the distribution channels for investment management services and mutual fund products. This strategy has contributed to a 12% increase in our share of the Canadian mutual fund market over the past two years.

United States

RBC Dain Rauscher

Minneapolis-based RBC Dain Rauscher comprises a full-service brokerage subsidiary and a fixed income business. RBC Dain Rauscher plans to grow through broadening and deepening relationships with existing clients by understanding their needs and the potential profitability of the client relationship. We also plan to grow by focusing on opportunities which generate greater market share and scale within our existing markets. The integration of Boston-based Tucker Anthony Sutro was completed in 2002 and made RBC Dain Rauscher the 9th-largest full-service securities firm in the U.S., with close to 2,000 financial consultants serving individual clients from coast to coast and a fixed income business with 280 investment bankers, sales representatives and traders serving institutional and retail clients nationwide.

International

RBC Global Private Banking

This internationally-focused unit provides private banking, trust and investment counselling solutions to high net worth clients in more than 100 countries. Our goal is to provide specialized global services to high net worth clients with assets of more than \$1 million. In 2003, we intend to grow revenues by leveraging CRM capabilities within the group, by exploring potential European and North and South American acquisitions, and by building alliances in markets where we already have a presence. The addition of non-proprietary money management capabilities will expand our value proposition to clients.

Financial highlights by division

RBC Investments' revenues grew 12% from last year for the reasons mentioned on page 32. The decline in revenues from the Canadian & International Brokerage group was due to lower transaction- and fee-based revenues, reflecting continued weakness in capital markets. Global Asset Management's revenues declined 57% as revenues in 2001 included a \$313 million gain on the sale of RT Capital Management and 10 months of results from that business that did not recur in 2002.

Revenues

| (C\$ millions) | % change | 2002 | 2001 |
|------------------------------------|----------|----------|----------|
| Canadian & International Brokerage | (9)% | \$ 984 | \$ 1,076 |
| RBC Dain Rauscher (1) | 106 | 1,702 | 827 |
| RBC Global Private Banking (2) | 5 | 678 | 643 |
| Global Asset Management (3) | (57) | 286 | 660 |
| Other (4) | (108) | (3) | 37 |
| | 12% | \$ 3,647 | \$ 3,243 |

- (1) 2002 revenues include Tucker Anthony Sutro acquired on October 31, 2001.
 (2) Includes both Canadian and international businesses and Financial Planning.
 (3) 2001 revenues included RT Capital Management until August 15, 2001 and a \$313 million gain on the sale of RT Capital Management.
 (4) 2001 revenues included a \$36 million gain on the sale of Group Retirement Services. Excluding this gain, 2001 revenues were \$1 million.

Despite difficult capital market conditions, our Canadian & International Brokerage group was able to grow its assets, with much of the growth coming from fee-generating assets. Higher AUA in RBC Global Private Banking were related to an increase in new business, the acquisition of the assets of Barclays Bank PLC's private banking operations in the Americas and a 5% increase in the value of the British pound against the Canadian dollar. These increases largely offset lower AUA at RBC Dain Rauscher, due to declines in market values, as well as an expected decrease related to broker attrition resulting from weak market conditions and the integration of Tucker Anthony Sutro into RBC Dain Rauscher.

Assets under administration

| (C\$ millions) | % change | 2002 | 2001 |
|--|----------|------------|------------|
| Personal | | | |
| Canadian & International Brokerage | 3% | \$ 111,340 | \$ 107,760 |
| RBC Dain Rauscher | (18) | 132,930 | 161,740 |
| RBC Global Private Banking | 21 | 82,390 | 67,990 |
| | (3) | 326,660 | 337,490 |
| Institutional – RBC Global Private Banking | 14 | 69,730 | 61,010 |
| | (1)% | \$ 396,390 | \$ 398,500 |

The decline in personal AUM largely reflected lower asset values due to weak capital market conditions. As part of the integration of Tucker Anthony Sutro into RBC Dain Rauscher, a non-core asset management business which was acquired as part of Tucker Anthony Sutro was divested, contributing to the decrease in personal AUM. Much of the increase in institutional AUM was related to the accumulation of new assets in RBC Global Private Banking and at RBC Dain Rauscher. Mutual fund asset levels remained relatively stable with lower market values offset by strong net sales driven by a successful RRSP campaign.

Assets under management

| (C\$ millions) | % change | 2002 | 2001 |
|----------------|----------|-----------|-----------|
| Personal | (23)% | \$ 35,660 | \$ 46,620 |
| Institutional | 9 | 18,410 | 16,940 |
| Mutual funds | (1) | 34,230 | 34,550 |
| | (10)% | \$ 88,300 | \$ 98,110 |

RBC Capital Markets

Business profile

RBC Capital Markets provides wholesale financial services to large corporate, government and institutional clients in North America and in specialized product and industry sectors globally. Headquartered in Toronto, RBC Capital Markets has key centres of expertise in Minneapolis, New York and London, and offices in 27 other cities.

Industry profile

The Canadian wholesale financial services market is mature and, as a result, many Canadian firms are seeking growth opportunities outside of their domestic market, primarily in the U.S. The U.S. capital markets are dominated by several large global investment banks whose principal focus is on the top tier of companies forming the S&P 500. However, we believe significant opportunities exist for specialized players targeting the lower end of the S&P 500. To succeed in the North American context requires the ability to provide clients with innovative, value-added solutions that reflect a keen understanding of both the company and industry sector. Increasingly, new business opportunities will accrue to those firms with a reputation for adhering to high ethical standards.

Our strengths

- Top-tier market shares in virtually all lines of business in Canada
- Established reputation as a premier Canadian investment dealer as evidenced by our market share leadership
- Superior origination and distribution capability as measured by our standings in underwriting league tables
- Expertise and market knowledge in a broad array of industries

Our strategy

Our goals are to be recognized as the leading corporate and investment bank in Canada based on external rankings and to build a successful integrated North American business, while continuing to expand our specialized global businesses.

Key strategies for RBC Capital Markets include the following:

- In Canada, to maintain our position as a leading full-service provider in all of our markets by continuing to leverage the breadth of our long-standing client relationships, the depth of our trading, research and sales capabilities, and the strength of our brand and reputation in the Canadian market
- In the U.S., to provide value-added solutions by offering clients a broad product portfolio delivered through specialized industry teams, with the goal of building an integrated North American franchise. We will leverage the depth of our research and advisory capabilities in targeted North American industry sectors, specifically energy, technology, communications, health care, consumer products, and mid-size financial institutions
- Continue to expand our global specialized businesses by providing clients with customized, value-added solutions in the areas of bonds, money markets, foreign exchange, structured finance and equity and credit derivatives

Outlook for 2003

Given our expectations for reasonable economic growth in both Canada and the U.S. and a moderate capital markets recovery in 2003, we are anticipating modest revenue growth in 2003. Our outlook is based on the expectation of a recovery in trading volumes, merger and acquisition activities and new issue and advisory mandates to more normalized levels. We intend to maintain our focus on strategic cost management and to keep the rate of expense growth below that of revenue growth. We also plan to continue to proactively manage the credit risk associated with our corporate loan portfolio.

Financial performance

Net income increased 26%, or 17% on a core basis, as expenses fell far more than did revenues. Core ROE was unchanged from 2001, with higher net income offset by \$700 million of additional common equity attributed to the segment compared to last year, reflecting a change in methodology for attributing capital relating to credit risk.

Revenues declined \$86 million or 3% from last year, due largely to lower trading revenues in our platform resulting from continued weakness in capital markets and lower lending revenues due to targeted reductions in the corporate loan portfolio.

Non-interest expense fell \$177 million or 10% due to a lower number of employees and reduced variable compensation costs. Retention compensation costs related to the acquisition of Dain Rauscher Wessels, fully integrated into RBC Capital Markets since early 2002, were also lower, falling to \$51 million from \$88 million in 2001.

The provision for credit losses increased by \$58 million or 14% from 2001, due primarily to certain telecommunication, cable and energy accounts that were classified as nonaccrual during the year. The increase in the provision for credit losses was partially offset by related credit derivative gains which were recorded in non-interest revenue. Nonaccrual loans were down \$20 million or 2% from last year, reflecting charge-offs in the corporate loan portfolio.

The decline in income taxes was attributable to the tax rate differentials in various jurisdictions, as well as higher income taxes in 2001 resulting from a special \$27 million income tax expense shown in Table 6 on page 27.

Results

| (C\$ millions, taxable equivalent basis, except percentage amounts) | % change | 2002 | 2001 |
|---|----------|----------|----------|
| Net interest income | 29% | \$ 553 | \$ 429 |
| Non-interest revenue | (9) | 2,142 | 2,352 |
| Gross revenues | (3) | 2,695 | 2,781 |
| Provision for credit losses | | | |
| Allocated specific | 14 | 465 | 407 |
| Total | 14 | 465 | 407 |
| Non-interest expense (1) | (10) | 1,627 | 1,804 |
| Net income before income taxes | 6 | 603 | 570 |
| Income taxes | (28) | 143 | 200 |
| Taxable equivalent adjustment | — | 21 | 21 |
| Net income | 26% | \$ 439 | \$ 349 |
| U.S. net income | n.m. | \$ (36) | \$ (77) |
| Net income as a % of total bank net income | 100 bp | 15% | 14% |
| ROE | 90 bp | 10.5% | 9.6% |
| Economic Profit | n.m. | \$ (55) | \$ (44) |
| Average assets | 13% | 180,700 | 159,500 |
| Average loans and acceptances | (6) | 28,800 | 30,700 |
| Average deposits | 10 | 81,100 | 73,600 |
| Average common equity | 21 | 4,000 | 3,300 |
| Core results (2) | | | |
| Net income | 17 | 439 | 376 |
| ROE | — | 10.5% | 10.5% |
| Credit information | | | |
| Nonaccrual loans | (2)% | \$ 1,094 | \$ 1,114 |
| Net charge-offs | 120 | 510 | 232 |
| Net charge-offs as a % of average loans and acceptances | 101 bp | 1.77% | .76% |
| Number of employees (full-time equivalent) | (1)% | 2,938 | 2,954 |

(1) Includes goodwill amortization expense of \$43 million in 2001 (nil in 2002).

(2) Excluding special items in 2001 detailed in Table 6 on page 27. Only the lines affected by special items are shown here.

n.m. not meaningful

Strategy by division

Capital Markets Services

This division was formed in November 2001, combining the equity research, sales and trading businesses with the corporate and investment banking businesses. We offer a full range of credit and corporate finance products, including debt and equity underwriting, mergers & acquisitions (M&A) advice and execution, and expertise in research and equity sales and trading activities.

In Canada, we will build on our key strengths – expert knowledge of the Canadian markets, breadth and longevity of client relationships, depth in trading, research and sales and a long-standing reputation as a top-ranked domestic investment bank – to continue to be a full-service provider to all industries.

On a North American basis, we will be industry-focused – specifically technology, telecommunication, health care, energy, consumer products and mid-size financial institutions. By leveraging our research and advisory capabilities, we expect to differentiate ourselves on our ability to provide superior knowledge of investment opportunities and market-based solutions for our target clients.

Global Financial Products

This division was formed in November 2001 to address the continuing convergence of financial products available to clients. Its formation brought together the business activities involving the origination, syndication, securitization, trading and distribution of debt products globally. These products include loans, bonds and derivatives at both the investment grade and sub-investment grade levels. As well, Global Financial Products provides leveraged product asset management capabilities and is the centre of expertise for RBC Capital Markets' proprietary trading activities. The combination of these businesses provides the ability to maximize internal expertise and deliver a broad array of value-added ideas and solutions to clients.

We intend to continue to focus on identifying opportunities where we can build from our existing strengths to provide solutions-based approaches to structuring transactions for our clients.

Global Treasury Services

Global Treasury Services combines our money markets and foreign exchange businesses and provides global clients with foreign exchange, commodities, derivatives and interest rate products, as well as currency risk management and advisory services. These products and services are delivered through our extensive global sales and trading network, operating from centres that include Toronto, London and New York. Recognized as a market leader in foreign exchange e-commerce solutions, we also deliver services through our Internet trading platform, FX Direct, and are a member of the multi-bank global trading platform, FXall. We will continue to invest in innovative electronic delivery channels that offer sophisticated and flexible products and services.

Global Credit

Global Credit provides centralized management of all credit exposure associated with our loan portfolio. While wholesale lending is fundamental to the attraction and expansion of high-margin client businesses, lending must be strategic in order to maximize the returns to shareholders. Our portfolio and transaction management specialists use sophisticated risk management and analytical tools designed to ensure that the pricing on loans is commensurate with the associated risk and reflects the value of all products and services a client has with RBC.

Our transaction specialists use appropriate structures to provide clients with value-added, as opposed to commoditized, credit solutions. We work closely with our distribution teams to further reduce the size of our corporate lending base, while continuing to enhance the quality of earnings from this source.

Alternative Investments

Alternative Investments was formed in June 2002 with a mandate to expand our wholesale asset management capabilities, which today include operations in hedge funds and private equity. The alternative asset business provides non-traditional investment opportunities to high net worth individuals, corporations and institutional clients. These investment options include private equity and hedge funds, and can extend to other vehicles such as leveraged buyouts, Collateralized Debt Obligations (CDOs) and managed futures. We are uniquely positioned to leverage our existing infrastructure and our superior product knowledge across other businesses within RBC who have strong relationships with our target client base.

Financial highlights by division

Revenues were up 3% from 2001. Factors contributing to this increase include strong performance in Canadian equity new issue and M&A business and credit derivative gains related to accounts that were classified as impaired during the year. These factors offset lower sales and trading revenues, weak performance in U.S. equity new issue and M&A business and a 9% decline in core lending revenues. Core lending revenues decreased due to tightened spreads and the targeted reduction in the corporate loan portfolio, which is also reflected in the 13% decline in average assets.

Results

| (C\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|--|----------|----------|----------|
| Gross revenues | 3% | \$ 1,064 | \$ 1,033 |
| Average assets | (13) | 13,600 | 15,700 |

Revenues were up 5% in 2002. Favourable interest rate trading environments during the year helped to fuel revenue and asset growth from our traditional bond and derivative businesses, as well as revenue growth from new initiatives developed in securitization, leveraged finance and asset management. Revenues from our proprietary trading activities were down slightly from 2001 levels. Overall, this business achieved strong performance despite difficult markets and business limitations resulting from the displacement of our New York operations after the events of September 11th.

Results

| (C\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|--|----------|--------|--------|
| Gross revenues | 5% | \$ 883 | \$ 839 |
| Average assets | 41 | 70,700 | 50,200 |

Revenues were down 19% from 2001, which was a record year. The foreign exchange businesses experienced increased volatility in foreign exchange rates and decreased volumes, while economic and interest rate uncertainty negatively affected the money markets businesses. However, the derivative-based businesses performed well and we continued to grow revenues through e-commerce channels.

Results

| (C\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|--|----------|--------|--------|
| Gross revenues | (19)% | \$ 510 | \$ 627 |
| Average assets | 5 | 78,500 | 75,100 |

Global Credit's 29% decline in revenues was mainly driven by net negative mark-to-market adjustments on credit derivatives and other financial instruments and targeted reductions in our non-core lending portfolio, which is reflected in the 25% decline in average assets. These decreases offset revenue growth from our structured lending business and our successful efforts to transition towards higher-value loan transactions with greater liquidity.

Results

| (C\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|--|----------|--------|--------|
| Gross revenues | (29)% | \$ 142 | \$ 201 |
| Average assets | (25) | 10,100 | 13,500 |

Revenues were up 19%, with strong results from our hedge fund business, which accounts for the majority of our revenues, and stable results from proprietary trading offsetting lower revenues from the Canadian equity derivatives business. Revenues from our merchant banking business were also lower due to lower capital gains and the writedowns of certain investments.

Results

| (C\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|--|----------|-------|-------|
| Gross revenues | 19% | \$ 96 | \$ 81 |
| Average assets | 56 | 7,800 | 5,000 |

RBC Global Services

Business profile

RBC Global Services offers specialized transaction processing services to business, commercial, corporate and institutional clients in domestic and select international markets. Key businesses include investment administration, correspondent banking, cash management, payments and trade finance. Our 50% interest in the Moneris Solutions merchant card processing joint venture is reported under RBC Global Services.

Industry profile

The industry is characterized by increasing consolidation as certain segments become more global. Monoline specialists and new market entrants compete against traditional financial institutions. Scale is increasingly important to support the significant investment in technology required to introduce new products and services, accommodate industry-driven infrastructure changes and enhance operational efficiencies.

Our strengths

- We have a leadership position in Canada in these businesses as measured by AUA and market share of number of client relationships
- We have strong client relationships as evidenced by our high rate of client retention and new business generated from existing clients
- We are recognized for quality of service as evidenced by our top rankings in third-party client surveys
- We continue to develop and deploy new technology and client service solutions
- We are able to leverage our market position by aligning the resources within RBC Global Services with the expertise of other RBC platforms to offer a superior integrated service to the market

Our strategy

Our goal is to maintain and enhance our leadership position in Canada while continuing to develop a competitive international presence. To meet our goal, we will:

- Build upon existing client relationships to develop new business in select domestic and international markets
- Grow the business through key alliances, acquisitions and partnerships and continue to leverage the Moneris Solutions joint venture
- Drive revenue growth by developing new products and selling higher-margin value-added services, such as securities lending and trade advisory
- Enhance our processing and systems platforms to deliver new capabilities, improve efficiencies and drive economies of scale
- Continue the shift to electronic payment products and services focusing on Web-based solutions.

Outlook for 2003

Although we expect interest rates to rise in the second half of 2003, they will likely remain low in historical terms, which will continue to have an unfavourable impact on our revenue growth in 2003. As our revenues earned on deposits and cash balances are highly dependent upon the interest rate environment, our net interest income growth may be adversely affected. At the same time, the expectation of a modest recovery in capital markets beginning in the second half of 2003 should have a favourable impact on revenues from foreign exchange and on fee revenues from higher AUA.

Financial performance

Net income declined 35% while core net income, excluding the gain on the formation of the Moneris Solutions joint venture in 2001, declined 8% from last year, partially reflecting an increase in the provision for credit losses.

ROE was 28.7% compared to core ROE of 34.7% in 2001. The decline in ROE reflects lower net income as well as a \$100 million increase in average common equity attributed to this segment in 2002. The higher common equity reflects the 50% interest in the Moneris Solutions joint venture and higher capital attribution for operating risk.

Revenues were down 6% from last year, reflecting lower interest income due to the low interest rate environment, as well as lower foreign exchange revenues, which more than offset a 10% increase in fee income. Core revenues (which exclude an \$89 million gain on the formation of the Moneris Solutions joint venture) were up 5%. Revenues were positively affected by the acquisition of Perpetual Fund Services (an Australian custody, investment administration and unit registry business) on July 31, 2001 and a change pertaining to the classification of services provided by us to Moneris Solutions, effective November 2001. Payments for services provided to Moneris Solutions are now being treated as revenues, whereas previously they were treated as cost recoveries. Excluding these factors, revenue decreased by 3%.

Expenses were \$63 million or 13% higher in 2002 due to the inclusion of a full year of Perpetual Fund Services as well as continued investments in technology. Excluding the acquisition of Perpetual Fund Services and the change in the classification of services provided by us to Moneris Solutions discussed above, expenses increased by 2%.

The increases in both the provision for credit losses and nonaccrual loans were associated with Argentine loans classified as nonaccrual during the year.

Results

| (C\$ millions, except percentage amounts) | % change | 2002 | 2001 |
|---|-----------|--------|--------|
| Net interest income | (8)% | \$ 136 | \$ 148 |
| Non-interest revenue | (5) | 672 | 710 |
| Gross revenues | (6) | 808 | 858 |
| Provision for credit losses | | | |
| Allocated specific | n.m. | 10 | (2) |
| Total | n.m. | 10 | (2) |
| Non-interest expense (1) | 13 | 548 | 485 |
| Net income before income taxes | (33) | 250 | 375 |
| Income taxes | (29) | 77 | 109 |
| Net income | (35)% | \$ 173 | \$ 266 |
| U.S. net income | (47) | \$ 9 | \$ 17 |
| Net income as a % of total bank net income | (500)bp | 6% | 11% |
| ROE | (2,060)bp | 28.7% | 49.3% |
| Economic Profit | (18)% | \$ 100 | \$ 122 |
| Average common equity | 20 | 600 | 500 |
| Core results (2) | | | |
| Gross revenues | 5 | 808 | 769 |
| Net income | (8) | 173 | 189 |
| ROE | (600)bp | 28.7% | 34.7% |
| Credit information | | | |
| Nonaccrual loans | 275% | \$ 30 | \$ 8 |
| Net charge-offs | (114) | (1) | 7 |
| Net charge-offs as a % of average loans and acceptances | (40)bp | (.05)% | .35% |
| Number of employees (full-time equivalent) | 1% | 2,571 | 2,557 |

(1) Includes goodwill amortization expense of \$8 million in 2001 (nil in 2002).
(2) Excluding special items in 2001 detailed in Table 6 on page 27. Only the lines affected by special items are shown here.
n.m. not meaningful

Strategy by division

Institutional & Investor Services

Institutional & Investor Services is Canada's largest custodian as measured by AUA, and a leading provider of investment administration services to corporate and institutional investors worldwide. We operate from 13 locations throughout the world, with a global custody network spanning 80 markets.

We plan to continue to leverage our leadership position in the Canadian market to expand internationally, with a focus on serving fund managers, financial institutions and private banks.

We expect to achieve growth in our fee-based revenue streams by:

- Selling newly developed products and services to existing clients
- Expanding our client offerings in Europe and Asia-Pacific
- Further exploring alliance and acquisition opportunities

Financial Institutions

A comprehensive range of correspondent banking services is provided to banks globally and to broker-dealers within Canada, including cash management, payments, clearing, trade, foreign exchange, derivatives lending, securities lending, custody and settlement, and structured financing.

Our goal is to leverage our leadership position in the Canadian dollar clearing market and our client relationships by:

- Identifying differentiated value-added solutions that address the unique needs of the different market segments
- Adding new revenue streams by introducing service offerings that integrate the new product developments of RBC Global Services with those of other business platforms

We will continue to monitor and actively manage our exposure to higher risk markets.

Treasury Management & Trade

Treasury Management & Trade provides cash management, payment and trade services to business, commercial, corporate and public sector segments. Our trade team provides Canadian and foreign importers and exporters with a variety of trade products, services and counsel. Our cash management group provides a range of solutions to clients that allow for more effective cash flow and integration with client processing. Through Moneris Solutions we provide merchants with credit and debit card transaction processing services.

Our goal is to continue to be the leading provider in Canada by retaining profitable client relationships and growing market share in strategic markets by:

- Introducing a market segmentation approach that accommodates the diverse needs of business markets
- Expanding the functionality of our Web-based delivery channel for both cash management and trade services
- Introducing new trade products and services as well as expanding trade alliances to meet clients' international trade requirements while effectively managing risk
- Leveraging our cash management sales and service leadership position

Financial highlights by division

Revenues grew \$3 million or 1% in 2002, as the positive impact of the Perpetual Fund Services acquisition and higher fee income offset lower revenues from foreign exchange and interest income, due to the low interest rate environment. AUA increased by 3% from 2001 due to new business, but the effect of equity market declines largely offset the additions.

Results

| (C\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|--|----------|---------|---------|
| Gross revenues | 1% | \$ 401 | \$ 398 |
| Assets under administration | 3 | 963,200 | 936,700 |

Revenues fell \$15 million or 13% from last year, primarily due to a decrease in interest income associated with the low interest environment. In addition, certain fee revenues were transferred from RBC Global Services to RBC Capital Markets in 2002, contributing to the decline in revenues. The decrease in average assets reflected strategic reductions in the size of our Latin American loan portfolio, which now totals \$146 million.

Results

| (C\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|--|----------|-------|--------|
| Gross revenues | (13)% | \$ 98 | \$ 113 |
| Average assets | (15) | 1,700 | 2,000 |
| Average deposits | — | 1,700 | 1,700 |

Revenues decreased \$38 million or 11% from 2001. Excluding the \$89 million gain on the formation of the Moneris Solutions joint venture in 2001, revenues increased \$51 million or 20%. This increase primarily reflected a change pertaining to the classification of services provided by us to Moneris Solutions, effective November 2001. Payment for services provided to Moneris Solutions are now being treated as revenues, whereas previously they were treated as cost recoveries. Excluding this factor, revenues increased 5%, reflecting growth in fee income.

Results

| (C\$ millions, taxable equivalent basis, volumes in thousands) | % change | 2002 | 2001 |
|--|----------|--------|--------|
| Gross revenues | (11)% | \$ 309 | \$ 347 |
| Core gross revenues (1) | 20 | 309 | 258 |
| Average deposits | 6 | 6,350 | 6,000 |
| Payment volumes (2) | 12 | 7,440 | 6,670 |
| Payment errors (per 10,000 payments) | (40) | .33 | .55 |

(1) Excluding special items in 2001 detailed in Table 6 on page 27.

(2) Restated to include payment types not previously included in 2001.

Financial priority: Revenue growth and diversification

Highlights

- Revenues up 7%
- Operating (core) revenues up 11%, reflecting acquisitions
- Excluding recent U.S. acquisitions, operating revenues unchanged
- Net interest income up 10%
- Net interest margin of 1.93%, down four basis points
- Non-interest revenue up 5% and core non-interest revenues up 11%
- Non-interest revenue 54% of total revenues

TABLE 7 Operating revenues

| (C\$ millions, taxable equivalent basis) | 2002 | 2001 | 2002 vs 2001 Increase (decrease) | |
|--|-----------|-----------|-------------------------------------|------|
| Net interest income | \$ 7,191 | \$ 6,529 | \$ 662 | 10% |
| Non-interest revenue | 8,579 | 8,155 | 424 | 5 |
| Total revenues (reported) | 15,770 | 14,684 | 1,086 | 7 |
| Less: Special items (1) | — | (445) | (445) | n.m. |
| Operating revenues | 15,770 | 14,239 | 1,531 | 11 |
| Less: Revenues of recent U.S. acquisitions (2) | (3,265) | (1,735) | 1,530 | 88 |
| Operating revenues, excluding recent U.S. acquisitions | \$ 12,505 | \$ 12,504 | \$ 1 | —% |

(1) Special items in 2001 are described in Table 6 on page 27. There were no special items for 2002.
(2) Represents revenues of RBC Centura (now includes Eagle Bancshares, RBC Mortgage for the purposes of this discussion and analysis and what was previously SFNB), RBC Liberty Insurance and RBC Dain Rauscher (includes Tucker Anthony Sutro) and excludes Dain Rauscher Wessels, which was integrated into RBC Capital Markets in early 2002.
n.m. not meaningful.

Total revenues were up \$1.1 billion or 7% from 2001. Operating, or core, revenues (which exclude \$445 million of gains from special items recorded in 2001) were up \$1.5 billion or 11% from a year ago.

As shown in the table above, revenues from recent U.S. acquisitions accounted for all of the growth in operating revenue. Excluding recent U.S. acquisitions, operating revenues were unchanged from a year ago. This compared to a decline in operating expenses of 5% (discussed in the Cost control section on page 42).

Net interest income

Net interest income was up 10% from 2001 to \$7.2 billion. The majority of the increase stemmed from recent U.S. acquisitions. If these acquisitions are excluded, net interest income would have been up 2% due to an increase in the amount of interest-earning assets, particularly residential mortgages, which more than offset a narrower spread on deposits.

As shown in Table 8 below, the net interest margin decreased by four basis points from last year to 1.93%, reflecting a narrower spread between the prime rate and core deposit funding costs resulting from a reduction in the average Canadian prime rate to 4.15% from 6.55% in 2001.

TABLE 8 Net interest income and margin

| (C\$ millions, except percentage amounts) | 2002 | 2001 | 2000 |
|---|------------|------------|------------|
| Average assets | \$ 371,700 | \$ 331,600 | \$ 284,100 |
| Net interest income (1) | 7,191 | 6,529 | 5,307 |
| Net interest margin (2) | 1.93% | 1.97% | 1.87% |

(1) Taxable equivalent basis.
(2) Net interest income, on a taxable equivalent basis, as a percentage of average assets.

Outlook

We are targeting core revenue growth of 5–8% in fiscal 2003, based on our expectations that capital market activity will pick up somewhat, interest rates in Canada will rise and the Canadian and U.S. economies will grow somewhat faster than in 2002.

TABLE 9 Net interest income on average assets and liabilities

| (C\$ millions, taxable equivalent basis, except percentage amounts) | Average balances (1) | | | Interest (2) | | | Average rate | | |
|--|----------------------|------------|------------|--------------|-----------|-----------|--------------|-------|-------|
| | 2002 | 2001 | 2000 | 2002 | 2001 | 2000 | 2002 | 2001 | 2000 |
| Assets | | | | | | | | | |
| Deposits with banks | | | | | | | | | |
| Canada | \$ 331 | \$ 427 | \$ 612 | \$ 6 | \$ 18 | \$ 22 | 1.81% | 4.22% | 3.59% |
| International | 15,395 | 16,168 | 13,888 | 476 | 813 | 802 | 3.09 | 5.03 | 5.77 |
| | 15,726 | 16,595 | 14,500 | 482 | 831 | 824 | 3.06 | 5.01 | 5.68 |
| Securities | | | | | | | | | |
| Trading account | 66,631 | 53,477 | 40,669 | 1,945 | 2,143 | 1,519 | 2.92 | 4.01 | 3.74 |
| Available for sale (3) | 25,583 | 21,623 | 19,471 | 1,170 | 1,170 | 1,107 | 4.57 | 5.41 | 5.69 |
| Held to maturity | — | — | 1,057 | — | — | 71 | — | — | 6.72 |
| | 92,214 | 75,100 | 61,197 | 3,115 | 3,313 | 2,697 | 3.38 | 4.41 | 4.41 |
| Assets purchased under reverse repurchase agreements | 35,463 | 29,591 | 21,729 | 651 | 1,163 | 1,078 | 1.84 | 3.93 | 4.96 |
| Loans (4) | | | | | | | | | |
| Canada | | | | | | | | | |
| Residential mortgage | 65,901 | 62,449 | 59,860 | 3,903 | 4,087 | 3,891 | 5.92 | 6.54 | 6.50 |
| Personal | 26,631 | 28,089 | 26,949 | 1,734 | 2,325 | 2,290 | 6.51 | 8.28 | 8.50 |
| Credit card | 4,354 | 4,586 | 3,559 | 519 | 556 | 405 | 11.92 | 12.12 | 11.38 |
| Business and government | 30,217 | 33,890 | 34,381 | 1,291 | 1,281 | 1,506 | 4.27 | 3.78 | 4.38 |
| | 127,103 | 129,014 | 124,749 | 7,447 | 8,249 | 8,092 | 5.86 | 6.39 | 6.49 |
| International | 41,846 | 33,232 | 24,927 | 3,016 | 3,783 | 3,446 | 7.21 | 11.38 | 13.82 |
| | 168,949 | 162,246 | 149,676 | 10,463 | 12,032 | 11,538 | 6.19 | 7.42 | 7.71 |
| Total interest-earning assets | 312,352 | 283,532 | 247,102 | 14,711 | 17,339 | 16,137 | 4.71 | 6.12 | 6.53 |
| Non-interest-bearing deposits with banks | 1,753 | 1,188 | 930 | | | | | | |
| Customers' liability under acceptances | 8,515 | 9,890 | 10,281 | | | | | | |
| Other assets | 51,365 | 39,025 | 27,724 | | | | | | |
| Allowance for credit losses | (2,285) | (2,035) | (1,937) | | | | | | |
| Total assets | \$ 371,700 | \$ 331,600 | \$ 284,100 | \$ 14,711 | \$ 17,339 | \$ 16,137 | 3.96% | 5.23% | 5.68% |
| Liabilities and shareholders' equity | | | | | | | | | |
| Deposits (5) | | | | | | | | | |
| Canada | \$ 111,880 | \$ 110,228 | \$ 107,533 | \$ 2,964 | \$ 4,712 | \$ 5,060 | 2.65% | 4.27% | 4.71% |
| International | 108,849 | 90,459 | 71,024 | 2,745 | 4,000 | 3,997 | 2.52 | 4.42 | 5.63 |
| | 220,729 | 200,687 | 178,557 | 5,709 | 8,712 | 9,057 | 2.59 | 4.34 | 5.07 |
| Obligations related to securities sold short | 19,563 | 16,358 | 14,195 | 797 | 654 | 656 | 4.07 | 4.00 | 4.62 |
| Obligations related to assets sold under repurchase agreements | 19,630 | 19,892 | 11,873 | 414 | 894 | 653 | 2.11 | 4.49 | 5.50 |
| Subordinated debentures | 7,089 | 6,972 | 5,129 | 406 | 410 | 344 | 5.73 | 5.88 | 6.71 |
| Other interest-bearing liabilities | 5,546 | 3,042 | 3,042 | 194 | 140 | 120 | 3.50 | 4.60 | 3.94 |
| Total interest-bearing liabilities | 272,557 | 246,951 | 212,796 | 7,520 | 10,810 | 10,830 | 2.76 | 4.38 | 5.09 |
| Non-interest-bearing deposits | 21,540 | 20,732 | 17,509 | | | | | | |
| Acceptances | 8,515 | 9,890 | 10,281 | | | | | | |
| Other liabilities | 50,526 | 38,092 | 30,811 | | | | | | |
| | 353,138 | 315,665 | 271,397 | 7,520 | 10,810 | 10,830 | 2.13 | 3.42 | 3.99 |
| Shareholders' equity | | | | | | | | | |
| Preferred | 1,682 | 2,036 | 1,978 | | | | | | |
| Common | 16,880 | 13,899 | 10,725 | | | | | | |
| Total liabilities and shareholders' equity | \$ 371,700 | \$ 331,600 | \$ 284,100 | \$ 7,520 | \$ 10,810 | \$ 10,830 | 2.02% | 3.26% | 3.81% |
| Net interest income as a % of total average assets | \$ 371,700 | \$ 331,600 | \$ 284,100 | \$ 7,191 | \$ 6,529 | \$ 5,307 | 1.93% | 1.97% | 1.87% |
| Net interest income as a % of total average interest-earning assets | | | | | | | | | |
| Canada | \$ 199,066 | \$ 186,480 | \$ 180,429 | \$ 6,537 | \$ 5,324 | \$ 4,796 | 3.28% | 2.85% | 2.66% |
| International | 113,286 | 97,052 | 66,673 | 654 | 1,205 | 511 | .58 | 1.24 | .77 |
| Total | \$ 312,352 | \$ 283,532 | \$ 247,102 | \$ 7,191 | \$ 6,529 | \$ 5,307 | 2.30% | 2.30% | 2.15% |

(1) Calculated on a daily basis.

(2) Interest income includes loan fees of \$321 million (2001 – \$328 million; 2000 – \$274 million). The taxable equivalent adjustment is based on the Canadian tax rate of 38.5% (2001 – 41.5%; 2000 – 42.8%) and U.S. federal tax rate of 39.5%.

(3) Tax-exempt securities had average balances of \$6,729 million (2001 – \$6,752 million; 2000 – \$2,848 million), interest earned of \$233 million (2001 – \$141 million; 2000 – \$63 million) and average rates of 3.46% (2001 – 2.09%; 2000 – 2.21%).

(4) Average balances include nonaccrual loans.

(5) Deposits include savings deposits with average balances of \$39 billion (2001 – \$38 billion; 2000 – \$34 billion), interest expense of \$.3 billion (2001 – \$.6 billion; 2000 – \$.7 billion) and average rates of .69% (2001 – 1.58%; 2000 – 2.06%). Deposits also include time deposits with average balances of \$47 billion (2001 – \$44 billion; 2000 – \$38 billion), interest expense of \$1.3 billion (2001 – \$2.0 billion; 2000 – \$2.0 billion) and average rates of 2.85% (2001 – 4.55%; 2000 – 5.26%).

TABLE 10 Change in net interest income

| (C\$ millions, taxable equivalent basis) | 2002 vs 2001 Increase (decrease) due to changes in | | | 2001 vs 2000 Increase (decrease) due to changes in | | |
|---|--|---------------------|---------------|--|---------------------|---------------|
| | average volume (1) | average rate (1) | Net change | average volume (1) | average rate (1) | Net change |
| Assets | | | | | | |
| Deposits with banks | | | | | | |
| Canada | \$ (3) | \$ (9) | \$ (12) | \$ (7) | \$ 3 | \$ (4) |
| International | (37) | (300) | (337) | 122 | (111) | 11 |
| Securities | | | | | | |
| Trading account | 459 | (657) | (198) | 507 | 117 | 624 |
| Available for sale | 196 | (196) | — | 118 | (55) | 63 |
| Held to maturity | — | — | — | (71) | — | (71) |
| Assets purchased under reverse repurchase agreements | 197 | (709) | (512) | 339 | (254) | 85 |
| Loans | | | | | | |
| Canada | | | | | | |
| Residential mortgage | 218 | (402) | (184) | 169 | 27 | 196 |
| Personal | (116) | (475) | (591) | 95 | (60) | 35 |
| Credit card | (28) | (9) | (37) | 123 | 28 | 151 |
| Business and government | (147) | 157 | 10 | (21) | (204) | (225) |
| International | 832 | (1,599) | (767) | 1,016 | (679) | 337 |
| Total interest income | \$ 1,571 | \$ (4,199) | \$ (2,628) | \$ 2,390 | \$ (1,188) | \$ 1,202 |
| Liabilities | | | | | | |
| Deposits | | | | | | |
| Canada | \$ 70 | \$ (1,818) | \$ (1,748) | \$ 124 | \$ (472) | \$ (348) |
| International | 701 | (1,956) | (1,255) | 962 | (959) | 3 |
| Obligations related to securities sold short | 130 | 13 | 143 | 93 | (95) | (2) |
| Obligations related to assets sold under repurchase agreements | (12) | (468) | (480) | 377 | (136) | 241 |
| Subordinated debentures | 7 | (11) | (4) | 112 | (46) | 66 |
| Other interest-bearing liabilities | 94 | (40) | 54 | — | 20 | 20 |
| Total interest expense | 990 | (4,280) | (3,290) | 1,668 | (1,688) | (20) |
| Net interest income | \$ 581 | \$ 81 | \$ 662 | \$ 722 | \$ 500 | \$ 1,222 |

(1) Volume/rate variance is allocated on the percentage relationship of changes in balances and changes in rates to the total net change in net interest income on a taxable equivalent basis.

Non-interest revenue

As shown in Table 11 on page 41, non-interest revenue was up \$424 million, or 5%, from 2001, while core non-interest revenues, which exclude special items shown in Table 6 on page 27, were up \$869 million or 11%, both reflecting recent U.S. acquisitions. Core non-interest revenues were up 12% in RBC Banking, 6% in RBC Insurance and 31% in RBC Investments, largely reflecting acquisitions. Core non-interest revenues were up 8% in RBC Global Services but were down 9% in RBC Capital Markets.

Excluding the impact of recent U.S. acquisitions, core non-interest revenues were down \$133 million or 2%.

Partially driven by recent U.S. acquisitions, capital market fees (consisting of fees from full-service brokerage, discount brokerage and the institutional business) were up 23%, deposit and payment service charges were up 17% and investment management and custodial fees were up 8%. Mortgage banking revenues (which relate to mortgages originated in the U.S.) rose 17%, mutual fund revenues were up 4% and securitization revenues were up 38%, reflecting \$3.7 billion of residential mortgage securitizations during the year. Card service revenues

declined 2%. Despite contributions from recent U.S. acquisitions, trading revenues were down 3%. Insurance revenues were also down 3% while credit fees declined 6%. Other non-interest revenue was up \$255 million, or 68%, partially as a result of a \$77 million increase in fee revenue at RBC Dain Rauscher for the provision of back office services to other brokerage firms and a \$61 million increase in mark-to-market gains for derivative and hedging activities. These mark-to-market gains are determined in accordance with Statement of Financial Accounting Standards, *Accounting for Derivative Instruments and Hedging Activities* (FAS 133).

Excluding the effect of recent U.S. acquisitions, deposit and payment service charges increased by \$82 million, securitization revenues increased by \$47 million, insurance revenues increased by \$16 million, mutual fund revenues increased by \$8 million, credit fees declined by \$17 million, capital market fees declined by \$23 million, investment management and custodial fees declined by \$77 million and trading revenues declined by \$302 million.

Non-interest revenues accounted for 54% of total revenues, unchanged from 2001.

TABLE 11 Non-interest revenue

| (C\$ millions, except percentage amounts) | | | | | |
|---|-----------------|-----------------|-----------------|-------------------------------------|-------------|
| | 2002 | 2001 | 2000 | 2002 vs 2001 Increase (decrease) | |
| Capital market fees | \$ 1,866 | \$ 1,523 | \$ 1,538 | \$ 343 | 23% |
| Trading revenues | 1,766 | 1,820 | 1,540 | (54) | (3) |
| Investment management and custodial fees | 1,179 | 1,096 | 860 | 83 | 8 |
| Deposit and payment service charges | 1,041 | 887 | 756 | 154 | 17 |
| Mutual fund revenues | 723 | 692 | 624 | 31 | 4 |
| Card service revenues | 285 | 290 | 420 | (5) | (2) |
| Foreign exchange revenues, other than trading | 277 | 300 | 299 | (23) | (8) |
| Insurance revenues | 255 | 263 | 151 | (8) | (3) |
| Mortgage banking revenues | 240 | 206 | — | 34 | 17 |
| Credit fees | 223 | 237 | 212 | (14) | (6) |
| Securitization revenues | 172 | 125 | 104 | 47 | 38 |
| Gain (loss) on disposal of premises and equipment | 15 | 22 | (16) | (7) | (32) |
| Loss on sale of securities | (95) | (128) | (11) | 33 | 26 |
| Other | 632 | 377 | 203 | 255 | 68 |
| Total core | 8,579 | 7,710 | 6,680 | 869 | 11 |
| Special items (1) | — | 445 | — | (445) | n.m. |
| Total | \$ 8,579 | \$ 8,155 | \$ 6,680 | \$ 424 | 5% |

(1) Special items in 2001 are described in Table 6 on page 27. There were no special items for 2000 and 2002.

n.m. not meaningful

TABLE 12 Trading revenues

| (C\$ millions) | | | | |
|------------------------------------|-----------------|-----------------|-----------------|--|
| | 2002 | 2001 | 2000 | |
| Net interest income (1) | \$ 127 | \$ (68) | \$ (365) | |
| Non-interest revenue (2) | 1,766 | 1,820 | 1,540 | |
| Total | \$ 1,893 | \$ 1,752 | \$ 1,175 | |
| By product | | | | |
| Equity | \$ 753 | \$ 684 | \$ 495 | |
| Fixed income and money markets (3) | 876 | 726 | 378 | |
| Foreign exchange contracts (4) | 263 | 340 | 301 | |
| Commodity and precious metals | 1 | 2 | 1 | |
| Total | \$ 1,893 | \$ 1,752 | \$ 1,175 | |

(1) Includes interest earned on trading securities and other cash instruments held in the trading portfolios less funding costs associated with trading-related derivative and security positions.

(2) Primarily includes realized and unrealized gains and losses on trading securities, derivative instruments and foreign exchange trading activities.

(3) Includes Canadian government securities and corporate debt instruments, swaps, interest rate options, interest rate futures, forward rate agreements.

(4) Includes foreign exchange spot, forward, futures and options contracts.

Trading revenues

Trading revenues include gains and losses on securities and derivatives that arise from market-making, sales and principal trading activities. These securities and derivative positions are marked-to-market on a daily basis. A description of trading revenues included in net interest income and non-interest revenue is provided in footnotes (1) and (2) in Table 12 above.

As shown in Table 12, total trading revenues were up \$141 million or 8% in 2002. This was partially due to the acquisition of Tucker Anthony Sutro on October 31, 2001. Proprietary trading activities are strictly managed in accordance with VAR and trading limits and we continue to conduct the majority of client-related trading in the major G7 markets and currencies.

Fixed income and money market trading revenues increased by \$150 million, or 21%, largely from increases in fixed income trading volumes due to the favourable interest rate environment provided by successive central bank rate cuts and increases in derivative trading activities. Equity trading revenues increased by \$69 million, or 10%, primarily due to the inclusion of revenues from Tucker Anthony Sutro. Foreign exchange contract trading revenues declined by \$77 million, or 23%, in part due to lower trading volumes caused by increased volatility in the foreign exchange markets.

Financial priority: Cost control

Highlights

- Non-interest expense up 6% from 2001 and core non-interest expense up 7%, reflecting recent U.S. acquisitions
- Operating non-interest expense excluding recent U.S. acquisitions down 5%, reflecting continued cost control efforts

As shown in the table below, non-interest expense was up \$603 million or 6% and core non-interest expense (i.e., excluding special items shown in Table 6 on page 27) was up \$694 million or 7% from 2001.

Operating non-interest expense (which excludes the special items mentioned in Table 6 on page 27, the costs of SARs and retention compensation associated with acquisitions) was up \$708 million or 8% in 2002.

Non-interest expense of recent U.S. acquisitions was \$2.7 billion, up \$1.1 billion in 2002. The large increase is primarily due to the inclusion of a full year of expenses for RBC Centura, which was acquired on June 5, 2001, and expenses relating to the acquisition of Tucker Anthony Sutro, which was acquired on October 31, 2001. Excluding recent U.S. acquisitions, operating non-interest expense was down \$411 million or 5% from 2001. Further excluding goodwill amortization expense not associated with recent U.S. acquisitions, operating non-interest expense was down \$261 million, or 3%, in 2002.

From a segment perspective, by excluding expenses of recent U.S. acquisitions, operating expenses for RBC Investments would have been down \$133 million or 8%, for RBC Banking down \$113 million or 3% and for RBC Insurance down \$10 million or 5%. The decline in RBC Banking's expenses reflects ongoing success with its cost control initiatives initially implemented in 1999, while the reduction in RBC Investments largely reflects lower variable compensation in the weaker capital markets environment and cost control efforts. The decrease in RBC Insurance expenses partially reflects the cessation of goodwill amortization on November 1, 2001.

Operating expenses for RBC Capital Markets were down \$140 million or 8%, whereas operating expenses at RBC Global Services were up \$63 million or 13%. The reductions at RBC Capital markets, similar to the reductions at RBC Investments, were the result of lower variable compensation and continuing cost control. The increase in RBC Global Services costs was affected by a change that became effective November 2001, pertaining to the classification of services provided by us to Moneris Solutions, a card processing joint venture in which we have a 50% interest. Payments for services provided to Moneris Solutions are now being treated as revenues, whereas previously they were treated as cost recoveries. Also, expenses were impacted by the July 2001 acquisition of Perpetual Fund Services. Excluding this acquisition, and

the change in classification of services provided to Moneris Solutions, operating expenses at RBC Global Services increased by 2%.

Human resources costs increased by \$589 million or 10% in 2002, largely the result of a \$464 million or 17% increase in salaries expense and a \$100 million or 14% increase in benefits expense. The increase in salaries expense is primarily due to the acquisition of RBC Centura and Tucker Anthony Sutro. Pension benefit expense increased by \$129 million this year primarily due to a decrease in the fair value of plan assets due to weak equity markets, settlement costs on pension-related matters with Royal Trust pension plan members and increases in the interest cost on the benefit obligation. Furthermore, our defined contribution pension expenses were higher due to changes to our U.S. plan design and the launch of our Canadian defined contribution plan.

Other postretirement benefits expense decreased by \$39 million this year primarily as a result of an \$87 million charge that was taken in 2001 following the review of certain pension and other related future benefit plans. No similar charge was taken this year.

Retention compensation costs declined by \$18 million to \$158 million despite the addition of \$45 million of retention compensation costs pertaining to Tucker Anthony Sutro. We expect total retention compensation costs to fall to approximately \$87 million in 2003 and \$53 million in 2004. SAR expenses rose slightly during the year. SARs are discussed in Note 16 on page 89, and their costs are determined based upon the change in our share price and the vesting, which occurs over time.

Communications costs increased by \$111 million or 16%, equipment costs were up \$81 million or 12% and occupancy costs increased by \$72 million or 10%. These increases largely relate to the inclusion of a full year of expenses for RBC Centura Bank, which was acquired on June 5, 2001 and Tucker Anthony Sutro, which was acquired on October 31, 2001.

Excluding expenses from recent U.S. acquisitions, equipment costs would have been up \$51 million or 9%, human resource costs down \$147 million or 3%, amortization of goodwill and other intangibles down \$147 million or 87%, other costs down \$121 million or 12%, occupancy costs down \$24 million or 4%, professional fees down \$23 million or 7% and communications costs would have been unchanged.

| TABLE 13 Operating non-interest expense | | | | |
|--|-----------|----------|-------------------------------------|------|
| (C\$ millions) | 2002 | 2001 | 2002 vs 2001 Increase (decrease) | |
| Non-interest expense | \$ 10,244 | \$ 9,641 | \$ 603 | 6% |
| Less: Special items (1) | — | (91) | (91) | n.m. |
| Core non-interest expense | 10,244 | 9,550 | 694 | 7 |
| Less: Costs of SARs | (27) | (23) | 4 | 17 |
| RBC Dain Rauscher retention compensation (2) | (158) | (176) | (18) | (10) |
| Operating expenses | 10,059 | 9,351 | 708 | 8 |
| Less: Non-interest expense of recent U.S. acquisitions (3) | (2,725) | (1,606) | 1,119 | 70 |
| Operating expenses, excluding recent U.S. acquisitions | 7,334 | 7,745 | (411) | (5) |
| Less: Amortization of goodwill not associated with recent U.S. acquisitions | — | (150) | (150) | n.m. |
| Operating expenses, excluding recent U.S. acquisitions and goodwill amortization | \$ 7,334 | \$ 7,595 | \$ (261) | (3)% |

(1) Special items in 2001 are described in Table 6 on page 27. There were no special items in 2002.
(2) Includes Dain Rauscher Wessels for both periods and Tucker Anthony Sutro in 2002 only.
(3) Represents non-interest expense of RBC Centura (now includes Eagle Bancshares, RBC Mortgage for the purposes of this discussion and analysis and what was previously SFNB), RBC Liberty Insurance and RBC Dain Rauscher (includes Tucker Anthony Sutro) including goodwill amortization expense of \$102 million in 2001 (nil in 2002), but excluding retention compensation costs and Dain Rauscher Wessels, which was integrated into RBC Capital Markets in early 2002.
n.m. not meaningful.

Outlook

In 2003, we expect to grow operating expenses at a lower rate than operating revenues.

TABLE 14 Non-interest expense

| (C\$ millions, except percentage amounts) | 2002 | 2001 | 2000 | 2002 vs 2001 Increase (decrease) | |
|--|-----------|----------|----------|-------------------------------------|------|
| Human resources | | | | | |
| Salaries | \$ 3,189 | \$ 2,725 | \$ 2,319 | \$ 464 | 17% |
| Variable compensation | 2,095 | 2,056 | 1,839 | 39 | 2 |
| Acquisition related retention compensation | 158 | 176 | — | (18) | (10) |
| Benefits | 794 | 694 | 485 | 100 | 14 |
| SARs | 27 | 23 | 52 | 4 | 17 |
| | 6,263 | 5,674 | 4,695 | 589 | 10 |
| Occupancy | | | | | |
| Net premises rent | 587 | 553 | 384 | 34 | 6 |
| Premises repairs and maintenance | 70 | 55 | 68 | 15 | 27 |
| Depreciation | 103 | 91 | 81 | 12 | 13 |
| Property taxes | 11 | 6 | 15 | 5 | 83 |
| Energy | 17 | 11 | 22 | 6 | 55 |
| | 788 | 716 | 570 | 72 | 10 |
| Equipment | | | | | |
| Office and computer rental and maintenance | 467 | 375 | 376 | 92 | 25 |
| Depreciation | 285 | 296 | 288 | (11) | (4) |
| | 752 | 671 | 664 | 81 | 12 |
| Communications | | | | | |
| Telecommunication | 350 | 283 | 225 | 67 | 24 |
| Marketing and public relations | 211 | 180 | 173 | 31 | 17 |
| Postage and courier | 121 | 108 | 170 | 13 | 12 |
| Stationery and printing | 108 | 108 | 127 | — | — |
| | 790 | 679 | 695 | 111 | 16 |
| Professional fees | 419 | 390 | 267 | 29 | 7 |
| Amortization of goodwill | — | 252 | 80 | (252) | n.m. |
| Amortization of other intangibles | 72 | 36 | 11 | 36 | 100 |
| Other | | | | | |
| Business and capital taxes | 129 | 171 | 134 | (42) | (25) |
| Travel and relocation | 144 | 121 | 85 | 23 | 19 |
| Employee training | 46 | 43 | 38 | 3 | 7 |
| Donations | 41 | 35 | 26 | 6 | 17 |
| Other | 800 | 762 | 363 | 38 | 5 |
| | 1,160 | 1,132 | 646 | 28 | 2 |
| Total core | 10,244 | 9,550 | 7,628 | 694 | 7 |
| Special items (1) | — | 91 | — | (91) | n.m. |
| Total | \$ 10,244 | \$ 9,641 | \$ 7,628 | \$ 603 | 6% |

(1) Special items in 2001 are described in Table 6 on page 27. There were no special items for 2000 and 2002.

n.m. not meaningful

Continuing our focus on cost control

The cost control initiatives undertaken in 2002 and in prior years are continuing to yield favourable results as reflected in the 5% decline in operating expenses, excluding recent U.S. acquisitions, shown in Table 13.

RBC Banking surpassed its stated objective of no non-interest expense growth in 2002, reducing non-interest expense by \$107 million or 3%, excluding recent U.S. acquisitions. Its success is due to favourable results from a number of initiatives, including the following.

Increasing focus on fraud prevention. This led to over \$50 million of savings realized this year.

Eliminating duplication and other process inefficiencies. As the result of integrating the credit card business into RBC Royal Bank's product and sales structure, over \$10 million in cost savings were realized during 2002.

Integration of certain functions of SFNB, RBC Builder Finance and RBC Mortgage into RBC Centura. The successful integration of certain functions resulted in the realization of 100% of the three-year cost savings target of US\$70 million, nearly two years ahead of schedule.

Integration of certain functions of RBC Centura into RBC Royal Bank. A portion of RBC Centura call centre services has been reallocated to the RBC Royal Bank call centres in Canada, whereby over half of RBC Centura inbound calls are now handled by call centres in Canada. RBC Centura is also expecting to realize over \$7 million of cost savings in 2003 from the integration of certain operations of Eagle Bancshares.

Moving into 2003, RBC Banking is developing a common business framework enabled by e-technologies. We believe that this streamlined model will drive transformational cost reductions by providing standardized and flexible solutions across segments, channels and products. This initiative is expected to generate cost savings commencing in 2004.

During 2002, RBC Insurance realized cost savings by insourcing the provision of technology and infrastructure support to the RBC Systems & Technology group and by outsourcing its payroll function to an external payroll service provider. Also, RBC Liberty Insurance completed the migration and consolidation of the business insurance software and outsourcing assets acquired from Genelco Incorporated, resulting in cost eliminations. RBC Liberty Insurance is also in the process of migrating to the desktop and server operating environments used by the rest of our enterprise. These changes will result in lower costs and will leverage best practices.

RBC Investments' cost-cutting program, initiated in 2001 to offset the effects of market weakness, will continue into 2003. This segment continues to seek ways to permanently reduce non-interest expense. For example, by working with the Institutional & Investor Services unit of RBC Global Services, RBC Global Private Banking was able to realize cost savings through the sourcing of its fund management processing.

RBC Dain Rauscher achieved cost savings from the continued integration of Tucker Anthony Sutro. Cost savings are being realized through a number of initiatives, including reducing overlapping positions and leveraging scale opportunities that already exist in RBC Dain Rauscher's platform. RBC Dain Rauscher also achieved cost savings through the rationalization of parts of its business in response to poor market conditions. To date, cost savings realized from these initiatives have exceeded US\$30 million. Cost savings pertaining to the completion of the integration of Tucker Anthony Sutro into RBC Dain Rauscher are expected to be another US\$30 million in 2003.

RBC Capital Markets maintained a focused cost control effort in 2002 in response to the continued weak market conditions. Expense reductions were achieved through the execution of a number of initiatives including continued integration of Capital Market Services businesses in Canada and the U.S., targeted reductions in costs associated with the management of our loan portfolio, technology support and technology capital expenditures. In 2003, RBC Capital Markets will continue its focus on cost control.

RBC Global Services is a scale business with relatively high fixed costs. To achieve cost savings, this segment is focusing on improving operational efficiency by increasing revenue to achieve economies of scale and through continued improvements in its technology infrastructure. Revenue increases will be achieved through organic revenue growth and targeted acquisitions. Acquisitions will provide opportunities for cost savings through integration.

In addition to each platform undertaking its own cost containment initiatives, we have an E² (efficiency and effectiveness) effort underway for RBC Financial Group. The primary thrust of the E² initiative is to eliminate duplication between platforms and to identify centres of expertise that can be leveraged to enhance operational efficiency and revenue growth. To date, this initiative has identified over 55 projects that could result in cost savings and additional revenue.

TABLE 15 Taxes

(C\$ millions, except percentage amounts)

| | 2002 | 2001 | 2000 |
|--------------------------------------|-----------------|-----------------|-----------------|
| Income taxes | | | |
| Consolidated statement of income | \$ 1,415 | \$ 1,350 | \$ 1,412 |
| Taxable equivalent adjustment | 40 | 32 | 28 |
| | 1,455 | 1,382 | 1,440 |
| Other taxes | | | |
| Goods and services and sales taxes | 224 | 221 | 208 |
| Payroll taxes | 245 | 237 | 188 |
| Provincial capital taxes | 107 | 146 | 108 |
| Property taxes (1) | 11 | 6 | 16 |
| Business taxes | 22 | 25 | 26 |
| Insurance premium taxes | 22 | 21 | 11 |
| | 631 | 656 | 557 |
| Total | \$ 2,086 | \$ 2,038 | \$ 1,997 |
| Effective income tax rate (2) | 32.0% | 34.7% | 38.8% |
| Effective total tax rate (3) | 41.0% | 44.5% | 47.3% |

(1) Includes amounts netted against non-interest revenue regarding investment properties.

(2) Income taxes reported in the consolidated statement of income, as a percentage of net income before income taxes.

(3) Total income taxes and other taxes as a percentage of net income before income taxes and other taxes expressed on a taxable equivalent basis.

Income and other taxes

Income and other taxes shown in Table 15 above were \$2,086 million in 2002, comprising income taxes of \$1,455 million (including a taxable equivalent adjustment) and other taxes of \$631 million. Income taxes increased by \$73 million from 2001, largely due to higher net income before tax. Other taxes declined by \$25 million largely as a result of a decrease in the amount of provincial capital taxes paid.

As shown above, the effective income tax rate decreased from 34.7% in 2001 to 32.0% in 2002, reflecting a reduction in federal and provincial tax rates in Canada.

In addition to the income and other taxes reported in the consolidated statement of income, the bank recorded income tax benefits of \$7 million in 2002 (\$451 million in 2001) in shareholders' equity as shown in Note 14 on page 87.

Financial priority: Strong credit quality

Highlights

- Business and government loans and acceptances decreased from 42% of total loans and acceptances in 2001 to 39%
- Nonaccrual loans down 7%
- Nonaccrual loans to total loans and acceptances down from 1.36% to 1.27%
- Provision for credit losses stable at \$1.1 billion
- Allocated specific provision ratio of .50%, down slightly from .52%
- Net charge-offs ratio of .71%, up from .55%
- Allowance for credit losses down slightly from \$2.4 billion to \$2.3 billion

Loan portfolio

During 2002, the loan portfolio performed well in a very challenging environment, reflecting changes we have made in credit practices over the last two years. In 2002, we continued our strategy of moving towards a lower-risk portfolio mix, which includes more residential mortgage loans and less corporate loans, which are riskier and more capital intensive. As shown in the charts below, business and government loans and acceptances decreased to 39% of total loans and acceptances in 2002 from 48% in 1998. This compares to a ratio of 42% in 2001.

We buy credit protection to offset losses that may result from the potential credit deterioration of particular counterparties and to manage exposure. As at October 31, 2002, we had \$1 billion of credit protection in place including \$.2 billion in each of the telecommunication, energy and financial services sectors.

The portion of our business and government credit exposure rated investment grade increased slightly during 2002 from 69% to 70%. Business and government includes our small business portfolio, which is generally rated lower than larger businesses.

Table 16 on page 47 and Table 21 on page 52 provide a detailed breakdown of loans and acceptances. Business and government loans and acceptances declined \$5.6 billion in Canada and \$1.4 billion internationally, with a \$2.3 billion reduction outside of the U.S., partially offset by a \$.9 billion increase in the U.S. The overall decrease is driven by the ongoing business strategy of exiting non-core client relationships in RBC Capital Markets. We do not engage in subprime lending in the U.S.

In Canada, there were no significant increases in any of the sectors other than the automotive sector where the increase was due to the reclassification of approximately \$.8 billion of loans from transportation and environment. The largest reduction was in energy (\$1.4 billion).

In the U.S., portfolio increases took place in energy (\$1.1 billion) and commercial real estate (\$.8 billion), partially offset by a decrease in industrial products (\$.5 billion). The largest share of the increase in the

energy sector was in power generation. The commercial real estate increase includes \$.2 billion of loans acquired as a result of the Eagle Bancshares acquisition.

Outside North America, loans decreased by \$2.3 billion, including reductions in financial services, energy and industrial products. The overall reductions reflect focused de-marketing of Asia-Pacific loans, including Japan.

Telecommunication loans outstanding globally decreased by 22% to \$1.7 billion at October 31, 2002. Non-investment grade telecommunication loans were \$.9 billion, down from 59% of the portfolio to 49%. Currently seven telecommunication loans are classified as nonaccrual, compared to six at October 31, 2001. Approximately 90% of the original nonaccrual amount has been charged-off or specifically provided for. This results in a nonaccrual amount of \$41 million, net of allowances, at the end of 2002.

At October 31, 2002, loans outstanding to the power generation sub-sector within the energy sector were \$2.0 billion, of which 48% were investment grade. The nonaccrual amount of \$74 million (net of allowances) related to three accounts.

For additional discussion of loans, see the Balance sheet and capital management section on page 58.

Nonaccrual loans

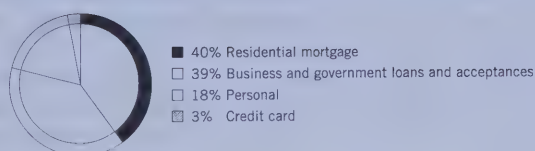
Loans are generally classified as nonaccrual, meaning the accrual of interest is discontinued, under conditions described in Note 1 on page 72.

As indicated in Table 17 on page 48, nonaccrual loans decreased \$177 million during the year to \$2,288 million. This decline reflects a slowdown in net additions (\$1,280 million versus \$1,912 million in 2001) and increased charge-offs (\$1,457 million versus \$1,125 million in 2001).

Nonaccrual loans decreased in both the consumer and the business and government loan portfolios.

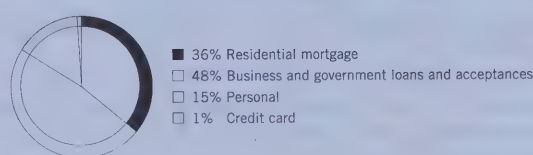
Breakdown of loans and acceptances portfolio (2002)

Significant change...



Breakdown of loans and acceptances portfolio (1998)

in portfolio mix



In the consumer portfolio, nonaccrual loans decreased by \$67 million to \$437 million. Canada saw a large decrease (\$75 million), resulting from overall portfolio improvement due to recent initiatives such as the implementation of an advanced risk modeling technology in order to optimize risk-reward and the optimization of credit policies and procedures (including the implementation of new origination models and new credit management and collection procedures).

Business and government nonaccrual loans fell \$110 million to \$1,851 million. This consisted of reductions in Canada (\$276 million) and the U.S. (\$50 million), offsetting increases in other international (\$216 million). Nonaccrual loans in the Canadian transportation and environment sector fell \$136 million due to a significant single name returning to performing status. There were also decreases in commercial real estate loans (\$72 million) and small business loans (\$56 million). The U.S. saw a net decrease resulting from reductions in the telecommunication sector (\$195 million), driven by significant charge-offs. This decrease was partially offset by an increase in the energy and media and cable sectors. Each of these two sectors was impacted by single individual accounts. New nonaccrual loans in Argentina contributed to an increase in other international.

Nonaccrual loans as a percentage of related loans and acceptances (before deducting the allowance for loan losses) decreased from 1.36% to 1.27%.

Provision for credit losses

The provision for credit losses is charged to income by an amount necessary to bring the allowance for credit losses to a level determined appropriate by management, as discussed in the Allowance for credit losses section below.

Outlook

In light of the continued economic and global political uncertainty that we face, we expect a specific provision for credit losses ratio of .45–.55% (using Canadian GAAP) in 2003, which is unchanged from our 2002 objective.

Allowance for credit losses

The allowance for credit losses is maintained at a level that management believes is sufficient to absorb probable losses in the loan and off-balance sheet portfolios. The individual elements as well as the overall allowance are evaluated on a quarterly basis. This evaluation is based on continuing assessments of problem accounts, recent loss experience and changes in other factors, including the composition and quality of the portfolio, economic conditions and regulatory requirements. The allowance is increased by the provision for credit losses, which is charged to income, and decreased by the amount of charge-offs net of recoveries.

The determination of the allowance for credit losses is based upon estimates derived from historical analysis, adjusted to take into account management's judgment relating to current assumptions. Therefore, the allowance for credit losses will inevitably differ from actual losses incurred in the future. To minimize these differences, management assesses the methodology and all significant assumptions on a regular basis.

The allowance for credit losses comprises three components – allocated specific, allocated general and unallocated – as described in Note 1 on page 73.

As shown in Table 19 on page 50, the allowance for credit losses decreased \$78 million or 3% between 2001 and 2002 to \$2,314 million. During the year, charge-offs, net of recoveries, were \$1,259 million or .71% of average loans and acceptances, versus \$940 million or .55% a year ago. The allocated country risk allowance of \$31 million has been eliminated as the result of the charge-off of the related fully provisioned loans.

The provision for credit losses was \$1,065 million in 2002, down \$54 million from 2001, as shown in Table 18 on page 49.

We acquire credit protection on portions of our portfolio by entering into credit derivative contracts. We also provide protection through credit derivatives to various counterparties. This year's provision for credit losses included amounts related to a telecommunication account and an energy account that were classified as nonaccrual and were partially offset by gains of \$102 million and \$13 million, respectively, on related credit derivatives. These amounts were recorded in non-interest revenues in accordance with FAS 133. We had also provided credit protection through derivatives to counterparties with respect to a large U.S. telecommunication company, which defaulted during the year, leading to a mark-to-market loss of \$69 million.

In the consumer portfolio, the allocated specific provision increased by \$25 million to \$430 million. Business and government loans showed a slight decrease of \$9 million to \$635 million. This comprises decreases in Canada of \$166 million, partially offset by increases in the U.S. of \$52 million and other international of \$105 million. The decreases in Canada are spread across various industries. In the U.S., there was an increase in the energy and information technology sectors, partially offset by decreases in commercial real estate and telecommunication. The increase in U.S. energy (\$107 million) is due to a single account.

The allocated specific provision amounted to .50% (.48% net of effect of credit derivatives) of average loans, acceptances and reverse repurchase agreements, down from .52% in 2001. Under Canadian GAAP, the ratio was .51%, down from .53% in 2001 and compared to a 2002 objective of .45–.55%.

In 2000, we entered into an agreement with an AAA rated reinsurer to provide capital if exceptional losses occur in the bank's loan portfolio. During the year, the reinsurer was downgraded from AAA. Based on this development and an internal review by management, the agreement was not renewed for fiscal 2003.

Credit risk concentrations

Concentration risk exists if a number of clients are engaged in similar activities, are located in the same geographic region or have comparable economic characteristics such that their ability to meet contractual obligations would be similarly affected by changes in economic, political or other conditions. Strategies to minimize concentration risk are discussed further under portfolio diversification in the Risk management section on page 55. In terms of geographic risk, Table 16 on page 47 shows that the largest domestic geographic exposure is in Ontario, comprising 35% of total loans and acceptances. Internationally, the largest concentration is in the U.S. where we have 16% of our total loans and acceptances.

As shown in Table 16 on page 47, excluding small business, the largest sector concentrations are in financial services, commercial real estate and energy, with 5%, 4% and 4% of loans and acceptances, respectively.

Table 20 on page 51 illustrates geographic risk concentrations of contractual amounts with clients outside of Canada. Only 11% of contractual amounts with clients are outside Canada and the U.S.

TABLE 16 Loans and acceptances (1)

| (C\$ millions, except percentage amounts) | 2002 | 2001 | 2000 | 1999 | 1998 | 2002 | 1998 |
|---|-------------------|-------------------|-------------------|-------------------|-------------------|-------------|-------------|
| Canada | | | | | | | |
| Atlantic provinces (2) | \$ 9,770 | \$ 9,654 | \$ 9,690 | \$ 8,840 | \$ 8,052 | 5.4% | 5.1% |
| Quebec | 15,190 | 13,863 | 16,191 | 14,936 | 14,066 | 8.5 | 8.9 |
| Ontario | 63,627 | 70,164 | 60,999 | 54,724 | 51,977 | 35.5 | 33.0 |
| Prairie provinces (3) | 26,989 | 25,192 | 29,402 | 25,521 | 23,288 | 15.0 | 14.8 |
| British Columbia | 23,367 | 22,696 | 25,118 | 23,141 | 22,295 | 13.0 | 14.2 |
| Total Canada | 138,943 | 141,569 | 141,400 | 127,162 | 119,678 | 77.4 | 76.0 |
| Consumer | | | | | | | |
| Residential mortgage | 67,700 | 64,066 | 61,444 | 58,524 | 55,836 | 37.7 | 35.5 |
| Personal | 25,918 | 27,202 | 27,207 | 24,353 | 21,814 | 14.5 | 13.9 |
| Credit card | 4,740 | 4,110 | 4,666 | 2,666 | 1,945 | 2.6 | 1.2 |
| | 98,358 | 95,378 | 93,317 | 85,543 | 79,595 | 54.8 | 50.6 |
| Business and government loans and acceptances | | | | | | | |
| Small business (4) | 9,470 | 9,788 | 11,701 | 10,334 | 8,452 | 5.3 | 5.4 |
| Agriculture | 4,427 | 4,758 | 4,931 | 4,217 | 3,851 | 2.5 | 2.5 |
| Financial services | 3,015 | 3,010 | 2,218 | 1,567 | 1,718 | 1.7 | 1.1 |
| Energy | 2,911 | 4,293 | 3,754 | 3,350 | 3,442 | 1.6 | 2.2 |
| Commercial mortgages | 2,468 | 2,635 | 2,961 | 2,635 | 2,434 | 1.4 | 1.5 |
| Commercial real estate | 2,393 | 2,325 | 2,594 | 2,400 | 2,523 | 1.3 | 1.6 |
| Consumer goods | 2,238 | 2,447 | 2,874 | 2,086 | 2,802 | 1.2 | 1.8 |
| Industrial products | 1,569 | 2,174 | 2,470 | 2,301 | 2,241 | .9 | 1.4 |
| Transportation and environment (5) | 1,450 | 2,138 | 1,519 | 1,562 | 1,392 | .8 | .9 |
| Automotive (5) | 1,370 | 864 | 673 | 611 | 698 | .8 | .4 |
| Government | 1,039 | 1,597 | 1,385 | 2,105 | 1,951 | .6 | 1.2 |
| Media and cable (6) | 994 | 1,510 | 1,120 | 1,135 | 959 | .5 | .6 |
| Forest products | 954 | 1,275 | 1,362 | 1,151 | 1,728 | .5 | 1.1 |
| Telecommunication | 487 | 677 | 1,008 | 525 | 361 | .3 | .2 |
| Mining and metals | 361 | 636 | 897 | 845 | 750 | .2 | .5 |
| Information technology | 191 | 203 | 210 | 191 | 204 | .1 | .1 |
| Other | 5,248 | 5,861 | 6,406 | 4,604 | 4,577 | 2.9 | 2.9 |
| | 40,585 | 46,191 | 48,083 | 41,619 | 40,083 | 22.6 | 25.4 |
| Total Canada | 138,943 | 141,569 | 141,400 | 127,162 | 119,678 | 77.4 | 76.0 |
| International | | | | | | | |
| United States | 29,192 | 25,944 | 13,415 | 13,060 | 13,717 | 16.3 | 8.7 |
| Europe, Middle East and Africa | 6,340 | 7,918 | 6,544 | 6,617 | 13,174 | 3.5 | 8.4 |
| Caribbean | 2,018 | 1,856 | 2,059 | 1,502 | 1,573 | 1.1 | 1.0 |
| Latin America | 1,400 | 1,680 | 1,842 | 2,309 | 3,875 | .8 | 2.5 |
| Asia | 1,004 | 1,328 | 1,781 | 2,417 | 4,550 | .5 | 2.9 |
| Australia and New Zealand | 677 | 805 | 771 | 983 | 825 | .4 | .5 |
| Total international | 40,631 | 39,531 | 26,412 | 26,888 | 37,714 | 22.6 | 24.0 |
| Consumer | | | | | | | |
| Residential mortgage | 5,142 | 3,378 | 1,540 | 718 | 632 | 2.9 | .4 |
| Personal | 6,038 | 5,309 | 812 | 902 | 947 | 3.3 | .6 |
| Credit card | 174 | 173 | — | — | — | .1 | — |
| | 11,354 | 8,860 | 2,352 | 1,620 | 1,579 | 6.3 | 1.0 |
| Business and government loans and acceptances | | | | | | | |
| Financial services | 6,542 | 9,347 | 7,912 | 6,937 | 10,896 | 3.6 | 6.9 |
| Energy | 3,731 | 2,994 | 3,051 | 3,887 | 4,702 | 2.1 | 3.0 |
| Commercial real estate | 5,124 | 4,082 | 271 | 464 | 862 | 2.9 | .6 |
| Consumer goods | 1,383 | 1,699 | 1,111 | 1,411 | 2,756 | .8 | 1.8 |
| Industrial products | 1,199 | 2,116 | 1,749 | 1,325 | 1,881 | .7 | 1.2 |
| Transportation and environment | 2,442 | 1,571 | 1,487 | 1,975 | 2,296 | 1.4 | 1.5 |
| Automotive | 411 | 527 | 513 | 878 | 2,264 | .2 | 1.4 |
| Government | 130 | 128 | 167 | 773 | 492 | .1 | .3 |
| Media and cable (6) | 1,321 | 1,380 | 2,033 | 1,909 | 2,270 | .7 | 1.4 |
| Forest products | 417 | 385 | 468 | 549 | 609 | .2 | .4 |
| Telecommunication | 1,246 | 1,558 | 2,244 | 1,206 | 1,756 | .7 | 1.1 |
| Mining and metals | 1,192 | 1,071 | 901 | 881 | 1,323 | .6 | .8 |
| Information technology | 180 | 396 | 433 | 709 | 1,212 | .1 | .8 |
| Other | 3,959 | 3,417 | 1,720 | 2,364 | 2,816 | 2.2 | 1.8 |
| | 29,277 | 30,671 | 24,060 | 25,268 | 36,135 | 16.3 | 23.0 |
| Total international | 40,631 | 39,531 | 26,412 | 26,888 | 37,714 | 22.6 | 24.0 |
| Total loans and acceptances | 179,574 | 181,100 | 167,812 | 154,050 | 157,392 | 100% | 100% |
| Allowance for loan losses | (2,203) | (2,278) | (1,871) | (1,884) | (2,026) | | |
| Total | \$ 177,371 | \$ 178,822 | \$ 165,941 | \$ 152,166 | \$ 155,366 | | |

(1) Based on residence of borrower.

(2) Includes Newfoundland and Labrador, Prince Edward Island, Nova Scotia and New Brunswick.

(3) Includes Manitoba, Saskatchewan and Alberta.

(4) Small business loans in 2002 comprises the following industries: commercial real estate of \$1,737 million (2001 – \$1,788 million); consumer goods of \$1,583 million (2001 – \$1,665 million); industrial products of \$887 million (2001 – \$916 million); transportation and environment of \$552 million (2001 – \$605 million); automotive of \$377 million (2001 – \$434 million); forest products of \$278 million (2001 – \$296 million); energy of \$125 million (2001 – \$157 million); information technology of \$93 million (2001 – \$133 million); mining and metals of \$69 million (2001 – n.a.); financial services of \$132 million (2001 – \$96 million); media and cable of \$77 million (2001 – \$84 million); telecommunication of \$34 million (2001 – \$45 million); and other of \$3,526 million (2001 – \$3,569 million).

(5) Commencing in 2002, certain amounts were reclassified from transportation and environmental sector grouping to the automotive group.

(6) Includes cable loans of \$267 million in Canada in 2002 (2001 – \$330 million; 2000 – \$262 million; 1999 – \$169 million; 1998 – \$164 million) and \$634 million internationally in 2002 (2001 – \$625 million; 2000 – \$1,321 million; 1999 – \$850 million; 1998 – \$1,221 million).

TABLE 17 Nonaccrual loans

(C\$ millions, except percentage amounts)

| | 2002 | 2001 | 2000 | 1999 | 1998 |
|--------------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Canada | | | | | |
| Atlantic provinces (1) | \$ 107 | \$ 124 | \$ 115 | \$ 77 | \$ 60 |
| Quebec | 90 | 282 | 198 | 259 | 261 |
| Ontario | 471 | 621 | 572 | 438 | 543 |
| Prairie provinces (2) | 177 | 143 | 129 | 198 | 161 |
| British Columbia | 427 | 453 | 355 | 415 | 485 |
| Total Canada | 1,272 | 1,623 | 1,369 | 1,387 | 1,510 |
| Consumer | | | | | |
| Residential mortgage | 102 | 142 | 185 | 173 | 166 |
| Personal | 275 | 310 | 247 | 236 | 217 |
| | 377 | 452 | 432 | 409 | 383 |
| Business and government | | | | | |
| Small business (3) | 205 | 261 | 248 | 232 | 130 |
| Agriculture (3) | 141 | 111 | 53 | 62 | 47 |
| Financial services | — | 7 | 20 | 16 | 121 |
| Energy | 1 | 27 | — | 38 | 6 |
| Commercial mortgages | 17 | 22 | 16 | 25 | 22 |
| Commercial real estate | 23 | 95 | 90 | 186 | 182 |
| Consumer goods | 47 | 11 | 37 | 43 | 55 |
| Industrial products | 23 | 45 | 28 | 19 | 25 |
| Transportation and environment | 138 | 274 | 185 | 21 | 13 |
| Automotive | 10 | 18 | 5 | 1 | 1 |
| Media and cable | 18 | 43 | 36 | 42 | 29 |
| Forest products | 199 | 195 | 184 | 233 | 383 |
| Telecommunication | 20 | — | — | 2 | 1 |
| Mining and metals | — | 1 | — | — | — |
| Information technology | 6 | 11 | 8 | 13 | 13 |
| Other | 47 | 50 | 27 | 45 | 99 |
| | 895 | 1,171 | 937 | 978 | 1,127 |
| Total Canada | 1,272 | 1,623 | 1,369 | 1,387 | 1,510 |
| International | | | | | |
| United States | 584 | 626 | 145 | 41 | 18 |
| Latin America | 217 | 14 | 9 | 10 | 4 |
| Europe, Middle East and Africa | 115 | 79 | 46 | 58 | 59 |
| Caribbean | 71 | 55 | 48 | 47 | 62 |
| Australia and New Zealand | 26 | 23 | — | — | — |
| Asia | 3 | 14 | 33 | 127 | 308 |
| | 1,016 | 811 | 281 | 283 | 451 |
| LDCs | — | 31 | 28 | 34 | 40 |
| Total international | 1,016 | 842 | 309 | 317 | 491 |
| Consumer | | | | | |
| Residential mortgage | 29 | 37 | 14 | 14 | 15 |
| Personal | 31 | 15 | — | — | — |
| | 60 | 52 | 14 | 14 | 15 |
| Business and government | | | | | |
| Financial services | 77 | 83 | 41 | 89 | 90 |
| Energy | 242 | 3 | 14 | 23 | 31 |
| Commercial real estate | 75 | 81 | 4 | 5 | 12 |
| Consumer goods | 10 | 19 | 2 | 18 | 119 |
| Industrial products | 30 | 10 | 83 | 38 | 76 |
| Transportation and environment | 68 | 91 | 56 | — | 1 |
| Automotive | 29 | 33 | — | 5 | 43 |
| Media and cable (4) | 56 | — | — | — | — |
| Telecommunication | 77 | 272 | — | — | — |
| Mining and metals | 128 | 40 | 11 | 11 | 8 |
| Information technology | 48 | 76 | — | — | — |
| Other | 116 | 82 | 84 | 114 | 96 |
| | 956 | 790 | 295 | 303 | 476 |
| Total international | 1,016 | 842 | 309 | 317 | 491 |
| Total (5), (6) | \$ 2,288 | \$ 2,465 | \$ 1,678 | \$ 1,704 | \$ 2,001 |

(1) Includes Newfoundland and Labrador, Prince Edward Island, Nova Scotia and New Brunswick.

(2) Includes Manitoba, Saskatchewan and Alberta.

(3) Includes government guaranteed portions of nonaccrual loans of \$64 million in small business in 2002 (2001 – \$95 million; 2000 – \$101 million; 1999 – \$79 million) and \$10 million in agriculture (2001 – \$6 million; 2000 – \$6 million; 1999 – \$5 million). Prior to 1999, only the non-guaranteed portion was considered nonaccrual.

(4) Consists entirely of cable nonaccrual loans.

(5) Includes foreclosed assets of \$32 million in 2002 (2001 – \$37 million; 2000 – \$16 million; 1999 – \$26 million; 1998 – \$28 million).

(6) Past due loans greater than 90 days not included in nonaccrual loans was \$217 million in 2002 (2001 – \$245 million).

TABLE 18 Provision for credit losses

(C\$ millions, except percentage amounts)

| | 2002 | 2001 | 2000 | 1999 | 1998 |
|--------------------------------------|-----------------|-----------------|---------------|---------------|---------------|
| Canada | | | | | |
| Atlantic provinces (1) | \$ 59 | \$ 63 | \$ 58 | \$ 32 | \$ 35 |
| Quebec | (5) | 43 | 22 | 71 | 63 |
| Ontario | 330 | 398 | 342 | 52 | 144 |
| Prairie provinces (2) | 86 | 81 | 64 | 95 | 53 |
| British Columbia | 59 | 104 | 40 | 192 | 132 |
| Total Canada | 529 | 689 | 526 | 442 | 427 |
| Consumer | | | | | |
| Residential mortgage | 3 | 8 | — | 4 | 9 |
| Personal | 266 | 265 | 301 | 172 | 171 |
| Credit card | 135 | 125 | 102 | 55 | 28 |
| | 404 | 398 | 403 | 231 | 208 |
| Business and government | | | | | |
| Small business | 110 | 164 | 105 | 113 | 48 |
| Agriculture | 22 | 20 | 4 | 2 | 4 |
| Financial services | (27) | (9) | — | 5 | 113 |
| Energy | 4 | 17 | (8) | 12 | 1 |
| Commercial mortgages | (5) | 7 | 2 | 8 | 6 |
| Commercial real estate | (15) | 15 | (17) | 9 | (30) |
| Consumer goods | 19 | 2 | 7 | 11 | 23 |
| Industrial products | (7) | 14 | 2 | (10) | (6) |
| Transportation and environment | (19) | 13 | 56 | 7 | (27) |
| Automotive | — | 17 | — | — | — |
| Media and cable | (7) | 13 | 12 | 8 | 4 |
| Forest products | 4 | 7 | (36) | 81 | 76 |
| Telecommunication | 59 | — | (1) | (32) | (29) |
| Mining and metals | (1) | — | (1) | 1 | — |
| Information technology | 3 | 3 | 8 | 8 | 5 |
| Other | (15) | 8 | (10) | (12) | 31 |
| | 125 | 291 | 123 | 211 | 219 |
| Total Canada | 529 | 689 | 526 | 442 | 427 |
| International | | | | | |
| United States | 440 | 377 | 99 | 45 | (7) |
| Latin America | 57 | 5 | 2 | 2 | (2) |
| Europe, Middle East and Africa | 38 | (1) | (9) | 21 | 10 |
| Caribbean | 6 | (6) | 3 | — | 3 |
| Australia and New Zealand | 5 | 4 | — | — | — |
| Asia | (10) | (19) | (50) | 20 | 124 |
| Total international | 536 | 360 | 45 | 88 | 128 |
| Consumer | | | | | |
| Residential mortgage | 7 | — | — | 1 | 1 |
| Personal | 15 | 5 | — | — | — |
| Credit card | 4 | 2 | — | — | — |
| | 26 | 7 | — | 1 | 1 |
| Business and government | | | | | |
| Financial services | 21 | (3) | (21) | 2 | 36 |
| Energy | 141 | (8) | (2) | — | 21 |
| Commercial real estate | 4 | 65 | 1 | 2 | (2) |
| Consumer goods | (2) | — | (7) | (10) | (5) |
| Industrial products | 5 | 3 | 34 | 31 | 9 |
| Transportation and environment | 21 | 8 | 42 | — | (1) |
| Automotive | 1 | 7 | (8) | (2) | 29 |
| Media and cable | — | 3 | — | — | — |
| Telecommunication | 202 | 272 | — | — | — |
| Mining and metals | 28 | — | 2 | 15 | — |
| Information technology | 41 | 7 | — | 3 | — |
| Other | 48 | (1) | 4 | 46 | 40 |
| | 510 | 353 | 45 | 87 | 127 |
| Total international | 536 | 360 | 45 | 88 | 128 |
| Allocated specific provision | 1,065 | 1,049 | 571 | 530 | 555 |
| Allocated country risk provision | — | — | — | — | (80) |
| Allocated general provision (3) | (22) | 205 | 73 | n.a. | n.a. |
| Total allocated provision (3) | 1,043 | 1,254 | 644 | n.a. | n.a. |
| Unallocated provision (3) | 22 | (135) | 47 | n.a. | n.a. |
| Total | \$ 1,065 | \$ 1,119 | \$ 691 | \$ 760 | \$ 575 |

(1) Includes Newfoundland and Labrador, Prince Edward Island, Nova Scotia and New Brunswick.

(2) Includes Manitoba, Saskatchewan and Alberta.

(3) The allocated general provision and the unallocated provision together totalled \$230 million in 1999 and \$100 million in 1998. These were not separated into the allocated general and unallocated components.

TABLE 19 Allowance for credit losses

(C\$ millions, except percentage amounts)

| | 2002 | 2001 | 2000 | 1999 | 1998 |
|---|-----------------|-----------------|-----------------|-----------------|-----------------|
| Allowance at beginning of year | \$ 2,392 | \$ 1,975 | \$ 1,900 | \$ 2,066 | \$ 2,118 |
| Provision for credit losses | 1,065 | 1,119 | 691 | 760 | 575 |
| Charge-offs | | | | | |
| Canada | | | | | |
| Residential mortgage | (11) | (15) | (11) | (14) | (17) |
| Personal | (381) | (394) | (372) | (236) | (163) |
| Credit card | (172) | (169) | (150) | (65) | (52) |
| Business and government | (330) | (296) | (225) | (524) | (250) |
| | (894) | (874) | (758) | (839) | (482) |
| International | | | | | |
| Residential mortgage | (1) | (9) | — | — | — |
| Personal | (17) | (7) | — | — | — |
| Credit card | (6) | (2) | — | — | — |
| Business and government | (506) | (233) | (81) | (229) | (29) |
| LDC exposures | (33) | — | — | (4) | (325) |
| | (563) | (251) | (81) | (233) | (354) |
| | (1,457) | (1,125) | (839) | (1,072) | (836) |
| Recoveries | | | | | |
| Canada | | | | | |
| Residential mortgage | — | — | — | 2 | 6 |
| Personal | 68 | 66 | 44 | 31 | 26 |
| Credit card | 37 | 44 | 48 | 10 | 24 |
| Business and government | 72 | 58 | 48 | 66 | 80 |
| | 177 | 168 | 140 | 109 | 136 |
| International | | | | | |
| Personal | 2 | 1 | — | — | — |
| Credit card | 1 | — | — | — | — |
| Business and government | 18 | 16 | 22 | 5 | 8 |
| | 21 | 17 | 22 | 5 | 8 |
| | 198 | 185 | 162 | 114 | 144 |
| Net charge-offs | (1,259) | (940) | (677) | (958) | (692) |
| Acquisition of Centura Banks | — | 157 | — | — | — |
| Acquisition of Eagle Bancshares | 18 | — | — | — | — |
| Adjustments | 98 | 81 | 61 | 32 | 65 |
| Allowance at end of year | \$ 2,314 | \$ 2,392 | \$ 1,975 | \$ 1,900 | \$ 2,066 |
| Allocation of allowance (1) | | | | | |
| Canada | | | | | |
| Residential mortgage | \$ 35 | \$ 45 | \$ 46 | \$ 53 | \$ 50 |
| Personal | 429 | 447 | 403 | 344 | 156 |
| Credit card | 147 | 147 | 88 | 60 | — |
| Business and government | 711 | 791 | 664 | 748 | 604 |
| | 1,322 | 1,430 | 1,201 | 1,205 | 810 |
| International | | | | | |
| Residential mortgage | 6 | 4 | 11 | 9 | 7 |
| Personal | 36 | 33 | — | — | — |
| Credit card | 5 | 5 | — | — | — |
| Business and government | 583 | 581 | 322 | 380 | 359 |
| | 630 | 623 | 333 | 389 | 366 |
| Allocated allowance for loan losses (2) | 1,952 | 2,053 | 1,534 | 1,594 | n.a. |
| Unallocated allowance for loan losses (2) | 251 | 225 | 337 | 290 | n.a. |
| Total allowance for loan losses | 2,203 | 2,278 | 1,871 | 1,884 | 2,026 |
| Allowance for off-balance sheet and other items (3) | 109 | 109 | 98 | — | — |
| Allowance for tax-exempt securities | 2 | 5 | 6 | 16 | 40 |
| Total allowance for credit losses | \$ 2,314 | \$ 2,392 | \$ 1,975 | \$ 1,900 | \$ 2,066 |
| Percentage of loans and acceptances to total loans and acceptances (4) | | | | | |
| Canada | | | | | |
| Residential mortgage | 38% | 35% | 37% | 38% | 36% |
| Personal | 14 | 15 | 16 | 16 | 14 |
| Credit card | 3 | 2 | 3 | 2 | 1 |
| Business and government | 21 | 24 | 28 | 28 | 28 |
| | 76 | 76 | 84 | 84 | 79 |
| International | 24 | 24 | 16 | 16 | 21 |
| Total | 100% | 100% | 100% | 100% | 100% |

- (1) As a result of a change in methodology in 1999, the allowance for loan losses in 2002, 2001, 2000 and 1999 includes amounts for the allocated general allowance, which have been allocated to loan categories. These amounts total \$1,060 million (2001 – \$1,076 million; 2000 – \$765 million; 1999 – \$790 million) and have been allocated as follows: for Canada – residential mortgage \$20 million (2001 – \$21 million; 2000 – \$18 million; 1999 – \$11 million), personal \$266 million (2001 – \$266 million; 2000 – \$207 million; 1999 – \$174 million), credit card \$147 million (2001 – \$147 million; 2000 – \$88 million; 1999 – \$60 million), business and government \$386 million (2001 – \$385 million; 2000 – \$321 million; 1999 – \$370 million), and for International – residential mortgage \$3 million (2001 – \$2 million; 2000 and 1999 – nil), personal \$22 million (2001 – \$26 million; 2000 and 1999 – nil), credit card \$5 million (2001 – \$5 million; 2000 and 1999 – nil), business and government \$211 million (2001 – \$224 million; 2000 – \$131 million; 1999 – \$175 million). The amounts prior to 1999 do not include the allocated general allowance.
- (2) The allocated general and the unallocated allowance totalled \$850 million in 1998. These were not separated into the allocated general and unallocated components prior to October 31, 1999.
- (3) Commencing in 2000, the allowance for off-balance sheet and other items was separated and reported under other liabilities. Previously, the amount was included in the allowance for loan losses.
- (4) Loans and acceptances in Canada include all loans and acceptances booked in Canada, regardless of the currency or residence of the borrower.

TABLE 20 Foreign outstandings (1)

| | 2002 | | 2001 | | 2000 | |
|---|-------------------|-------------------|-------------------|-------------------|------------------|-------------------|
| | | % of total assets | | % of total assets | | % of total assets |
| (C\$ millions, except percentage amounts) | | | | | | |
| United States – Banks | \$ 5,838 | | \$ 7,186 | | \$ 5,462 | |
| Government | 3,257 | | 3,834 | | 889 | |
| Other | 62,210 | | 49,172 | | 30,034 | |
| | 71,305 | 18.67% | 60,192 | 16.61% | 36,385 | 12.38% |
| Western Europe | | | | | | |
| United Kingdom – Banks | 7,179 | | 6,275 | | 4,347 | |
| Government | 295 | | 153 | | 26 | |
| Other | 5,719 | | 5,256 | | 5,791 | |
| | 13,193 | 3.45 | 11,684 | 3.22 | 10,164 | 3.46 |
| France – Banks | 2,061 | | 2,378 | | 2,379 | |
| Government | 86 | | 68 | | 45 | |
| Other | 831 | | 1,176 | | 1,552 | |
| | 2,978 | .78 | 3,622 | 1.00 | 3,976 | 1.35 |
| Germany – Banks | 5,344 | | 5,952 | | 5,471 | |
| Government | 318 | | 173 | | 1 | |
| Other | 381 | | 559 | | 643 | |
| | 6,043 | 1.58 | 6,684 | 1.84 | 6,115 | 2.08 |
| Netherlands | 2,271 | .59 | 2,218 | .61 | 1,300 | .44 |
| Switzerland | 1,714 | .45 | 1,362 | .38 | 1,687 | .57 |
| Other | 5,658 | 1.49 | 5,244 | 1.45 | 4,305 | 1.47 |
| | 31,857 | 8.34 | 30,814 | 8.50 | 27,547 | 9.37 |
| Central/Eastern Europe, Middle East and Africa | 247 | .06 | 469 | .13 | 645 | .22 |
| Latin America | | | | | | |
| Argentina | 146 | .04 | 193 | .06 | 324 | .11 |
| Brazil | 38 | .01 | 71 | .02 | 75 | .02 |
| Chile | 800 | .21 | 836 | .23 | 751 | .26 |
| Mexico | 493 | .13 | 696 | .19 | 343 | .12 |
| Other | 42 | .01 | 174 | .05 | 212 | .07 |
| | 1,519 | .40 | 1,970 | .55 | 1,705 | .58 |
| Caribbean | | | | | | |
| Bahamas | 1,453 | .38 | 1,520 | .42 | 1,549 | .53 |
| Other | 485 | .13 | 1,902 | .52 | 1,952 | .66 |
| | 1,938 | .51 | 3,422 | .94 | 3,501 | 1.19 |
| Asia | | | | | | |
| Japan – Banks | 321 | | 53 | | 634 | |
| Government | 2,426 | | 1,663 | | 1,599 | |
| Other | 64 | | 988 | | 1,000 | |
| | 2,811 | .74 | 2,704 | .75 | 3,233 | 1.10 |
| Singapore | 229 | .06 | 217 | .06 | 336 | .11 |
| South Korea | 405 | .11 | 449 | .12 | 338 | .11 |
| Other | 38 | .01 | 145 | .04 | 188 | .07 |
| | 3,483 | .92 | 3,515 | .97 | 4,095 | 1.39 |
| Australia and New Zealand | 2,842 | .74 | 2,335 | .64 | 1,775 | .60 |
| Allowance for loan losses (2) | (760) | (.20) | (728) | (.20) | (441) | (.15) |
| Total | \$ 112,431 | 29.44% | \$ 101,989 | 28.14% | \$ 75,212 | 25.58% |

- (1) Includes contractual amounts with clients in a foreign country related to: loans, accrued interest, acceptances, interest-bearing deposits with banks, securities, other interest-earning investments and other monetary assets including net revaluation gains on foreign exchange and derivative products. Local currency outstandings, whether or not hedged or funded by local currency borrowings, are included in country exposure outstandings. Foreign outstandings are reported based on location of ultimate risk.
- (2) The allowance for loan losses includes the international component of the allocated specific, allocated general and unallocated allowance. For years prior to 2002, the allowance for loan losses also includes the allocated country risk allowance.

TABLE 21 U.S. loans and acceptances and loan quality information ⁽¹⁾

| (C\$ millions) | Loan balance | | | Nonaccrual loans | | | Provision for credit losses | | |
|--|--------------|-----------|-----------|------------------|--------|--------|-----------------------------|--------|-------|
| | 2002 | 2001 | 2000 | 2002 | 2001 | 2000 | 2002 | 2001 | 2000 |
| Consumer | | | | | | | | | |
| Residential mortgage | \$ 4,353 | \$ 2,666 | \$ 845 | \$ 16 | \$ 24 | \$ - | \$ 7 | \$ 8 | \$ - |
| Personal | 5,269 | 4,621 | 78 | 31 | 15 | - | 15 | 5 | - |
| Credit card | 125 | 128 | - | - | - | - | 4 | 2 | - |
| | 9,747 | 7,415 | 923 | 47 | 39 | - | 26 | 15 | - |
| Business and government loans and acceptances | | | | | | | | | |
| Financial services | 3,770 | 4,104 | 4,521 | 46 | 30 | - | 11 | 7 | - |
| Energy | 2,680 | 1,613 | 1,582 | 95 | - | - | 107 | - | - |
| Commercial real estate | 4,531 | 3,773 | 44 | 75 | 81 | 4 | 5 | 66 | 2 |
| Consumer goods | 958 | 1,172 | 435 | 10 | 9 | - | 4 | 2 | - |
| Industrial products | 974 | 1,513 | 1,107 | 30 | 8 | 68 | 8 | 3 | 40 |
| Transportation and environmental | 484 | 788 | 469 | 36 | 48 | 56 | 5 | (4) | 42 |
| Automotive | 409 | 408 | 221 | 29 | 33 | - | 1 | 6 | - |
| Government | 19 | 23 | - | - | - | - | - | - | - |
| Media and cable (2) | 1,107 | 1,038 | 1,782 | 56 | - | - | - | 3 | - |
| Forest products | 223 | 98 | 181 | - | - | - | - | - | - |
| Telecommunication | 689 | 835 | 1,131 | 77 | 272 | - | 202 | 272 | - |
| Mining and metals | 70 | 45 | 104 | - | - | - | - | - | - |
| Information technology | 177 | 299 | 374 | 48 | 76 | - | 41 | 7 | - |
| Other | 3,354 | 2,820 | 541 | 35 | 30 | 17 | 30 | - | 15 |
| | 19,445 | 18,529 | 12,492 | 537 | 587 | 145 | 414 | 362 | 99 |
| | \$ 29,192 | \$ 25,944 | \$ 13,415 | \$ 584 | \$ 626 | \$ 145 | \$ 440 | \$ 377 | \$ 99 |

(1) Based on residence of the borrower.

(2) Includes cable loans of \$522 million (2001 - \$455 million; 2000 - \$1,162 million) and cable gross nonaccrual loans of \$56 million in 2002.

TABLE 22 Risk profile

| (C\$ millions, except percentage amounts) | 2002 | 2001 | 2000 | 1999 | 1998 |
|--|----------|----------|----------|----------|----------|
| Nonaccrual loans | | | | | |
| Beginning of year | \$ 2,465 | \$ 1,678 | \$ 1,704 | \$ 2,001 | \$ 1,819 |
| Net additions | 1,280 | 1,912 | 813 | 743 | 628 |
| Charge-offs and adjustments | (1,457) | (1,125) | (839) | (1,040) | (446) |
| End of year | \$ 2,288 | \$ 2,465 | \$ 1,678 | \$ 1,704 | \$ 2,001 |
| As a % of related loans and acceptances (1) | | | | | |
| Canada | | | | | |
| Residential mortgage | .15% | .22% | .30% | .30% | .30% |
| Personal | 1.06 | 1.14 | .91 | .97 | .99 |
| Business and government | 2.36 | 2.75 | 1.97 | 2.24 | 2.52 |
| International | .93 | 1.18 | .97 | 1.07 | 1.21 |
| | 2.34 | 1.95 | 1.15 | 1.28 | 1.49 |
| Total | 1.27% | 1.36% | 1.00% | 1.11% | 1.27% |
| Allowance for credit losses | | | | | |
| Allocated specific | \$ 894 | \$ 951 | \$ 747 | \$ 786 | \$ 1,176 |
| Allocated country risk | - | 31 | 28 | 34 | 40 |
| Allocated general (2), (4) | 1,169 | 1,185 | 863 | 790 | n.a. |
| Total allocated (2) | 2,063 | 2,167 | 1,638 | 1,610 | n.a. |
| Unallocated (2) | 251 | 225 | 337 | 290 | n.a. |
| Total | \$ 2,314 | \$ 2,392 | \$ 1,975 | \$ 1,900 | \$ 2,066 |
| As a % of loans and acceptances | 1.2% | 1.3% | 1.1% | 1.2% | 1.3% |
| As a % of loans, acceptances and reverse repurchase agreements | 1.0% | 1.0% | 1.0% | 1.1% | 1.1% |
| As a % of nonaccrual loans (coverage ratio), excluding LDCs | 96% | 93% | 112% | 112% | 103% |
| Provision for credit losses | | | | | |
| Allocated specific | \$ 1,065 | \$ 1,049 | \$ 571 | \$ 530 | \$ 555 |
| Allocated country risk | - | - | - | - | (80) |
| Allocated general (3) | (22) | 205 | 73 | n.a. | n.a. |
| Total allocated (3) | 1,043 | 1,254 | 644 | n.a. | n.a. |
| Unallocated (3) | 22 | (135) | 47 | n.a. | n.a. |
| Total | \$ 1,065 | \$ 1,119 | \$ 691 | \$ 760 | \$ 575 |
| Allocated specific provisions as a % of average loans, acceptances and reverse repurchase agreements | .50% | .52% | .31% | .30% | .31% |
| Provision as a % of average loans, acceptances and reverse repurchase agreements | .50 | .55 | .38 | .43 | .32 |
| As a % of related average loans and acceptances | | | | | |
| Canada | | | | | |
| Residential mortgage | -.% | .01% | -.% | .01% | .02% |
| Personal | 1.00 | .94 | 1.12 | .71 | .76 |
| Credit card | 3.10 | 2.73 | 2.87 | 2.39 | 1.39 |
| Business and government | .32 | .67 | .28 | .49 | .51 |
| International | .39 | .50 | .39 | .35 | .35 |
| | 1.28 | 1.08 | .18 | .31 | .37 |
| Total allocated specific provision | .60% | .61% | .36% | .34% | .36% |
| Total provision for credit losses | .60 | .65 | .43 | .49 | .37 |
| Net charge-offs (excluding LDCs) as a % of average loans and acceptances | .69% | .55% | .42% | .61% | .24% |
| Net charge-offs as a % of average loans and acceptances | .71% | .55% | .42% | .62% | .45% |

(1) Loans and acceptances in Canada include all loans and acceptances booked in Canada, regardless of the currency or residence of the borrower.

(2) The allocated general and the unallocated amounts totalled \$850 million in 1998. These were not separated into the allocated general and unallocated components. The amounts prior to 1999 do not include the allocated general allowance.

(3) The allocated general provision and the unallocated provision totalled \$230 million in 1999, \$100 million in 1998. These were not separated into the allocated general and unallocated components.

(4) Includes the allowance for off-balance sheet and other items.

Risk management

Overview

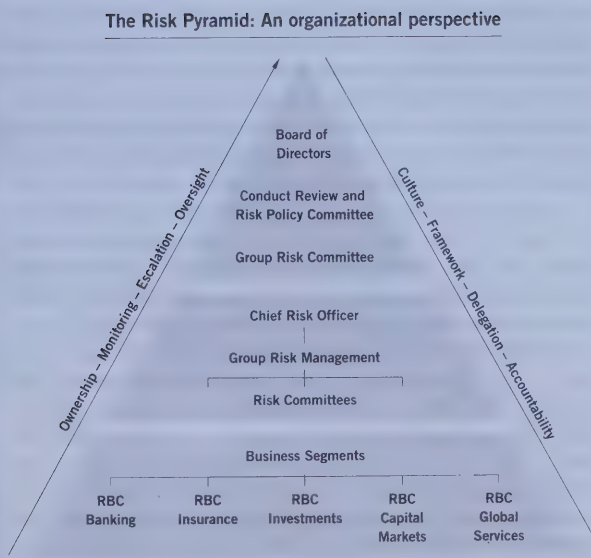
The risk management function strives to build shareholder value through leadership in the strategic management of risk. Priorities include:

- Enhancing communication on risk and risk appetite throughout the organization
- Aligning the risk management function with our business segments
- Investing in our capabilities to better measure, understand and manage risk
- Strengthening the efficiency, accessibility and responsiveness of key risk processes and practices
- Attracting, developing and retaining a team of highly performing professionals

Our business activities expose us to the risks outlined in the risk pyramid below. We use the risk pyramid as the primary tool to identify and assess risk across the organization. It provides a common language for evaluating risk in business reviews, new business, new products, new initiatives, acquisitions or alliances. We pay particular attention to the more control-able risks along the bottom of the pyramid.



- **Credit risk** is the risk of loss due to a counterparty's inability to fulfill its payment obligations. It also refers to a loss in market value due to the deterioration of a counterparty's financial position. A counterparty may be an issuer, debtor, borrower, policyholder, reinsurer or guarantor.
- **Market risk** is the risk of loss that results from changes in interest rates, foreign exchange rates, equity prices and commodity prices.
- **Liquidity risk** is the risk that we are unable to generate or obtain sufficient cash or equivalents on a cost-effective basis to meet our commitments as they fall due.
- **Insurance risk**, relative to our insurance platform, is the risk inherent in the development, issuance and administration of insurance policies, and includes product design and pricing risk, claims administration risk, underwriting risk and liability risk.
- **Operational risk** is the risk of direct or indirect loss resulting from inadequate or failed technology, human performance, processes or external events. The impact of operational risk can be financial loss, loss of reputation, loss of competitive position or legal and regulatory proceedings.



An organizational perspective

The cornerstone of effective risk management is a strong risk management culture, supported by numerous strategy and policy development processes, run jointly by risk management professionals and the business segments. This partnership is designed to ensure strategic alignment of business, risk and resource issues.

Risk management professionals work in partnership with the business segments and functional units to identify risks, which are then measured, monitored and managed. In line with a group-wide portfolio management approach, portfolio analytical techniques are employed in an effort to optimize the risk-reward profile and ensure the efficient allocation of capital.

A structure of management and board committees provides oversight of the risk management process.

The Board of Directors and Group Risk Committee

The top level of the organizational perspective risk pyramid on page 53 comprises the Board of Directors, the Conduct Review and Risk Policy Committee and Group Risk Committee. Key responsibilities are to:

- Shape, influence and communicate the organization's risk culture
- Determine and communicate the organization's risk appetite
- Define the organizational structure for Group Risk Management
- Review and approve policies for controlling risk
- Review and monitor the major risks being assumed by, or facing, the organization, providing direction as required
- Ensure there are sufficient and appropriate risk management resources across the organization against the risks being taken

Risk management

The middle level of the organizational perspective risk pyramid on page 53 comprises the Chief Risk Officer, Group Risk Management and the various Risk Committees. The Risk Committees include the Asset/Liability Committee, U.S. Corporate Governance Committee, the Ethics and Compliance Committee, Risk Management Committee and other committees responsible for areas such as interest rate risk and trading risk. During 2002, the SPE Risk Committee was established with a mandate to review and report on the activities of SPEs. This Committee reports jointly to the Chief Risk Officer and the Chief Financial Officer to ensure compliance with SPE policies and procedures across the enterprise. See page 64 for further discussion of SPEs.

Key responsibilities are to:

- Implement and maintain an integrated enterprise-wide risk measurement, management and reporting framework
- Establish a comprehensive risk assessment and approval process including enterprise-wide policies and procedures
- Establish guidelines and risk limits to ensure appropriate risk diversification and optimization of risk-return on both a portfolio and transactional basis
- Advise the board and executive management of major risks being assumed by, or facing, the organization
- Partner with the business segments in identifying, understanding, measuring, mitigating and monitoring the risks being taken

Economic Capital

Economic Capital (EC) is an estimate of the amount of equity required to underpin risks. It is calculated by determining the level of capital that is necessary to cover risks consistent with our desired solvency standard and debt ratings. EC analysis is intended to represent the shareholder's perspective and drives the optimization of shareholder returns. Calculation of EC involves a number of judgments and assumptions, and changes to them may result in different amounts of EC being computed. EC is attributed to provide directly comparable performance measurements for each of our business activities and assist senior management in strategic planning, resource allocation and performance measurement. Capital attribution methodologies are continuously monitored to ensure risks are being consistently quantified utilizing all available information. Periodically, enhancements are made to these methodologies with the changes applied prospectively.

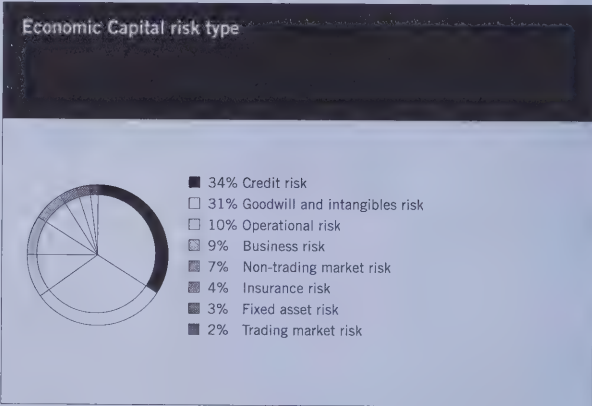
EC attribution methodology aims to:

- Cover all risks
- Ensure that a dollar of capital represents the same amount of risk wherever attributed
- Determine capital requirements in an unbiased accurate manner
- Create economically rational incentives for business managers

EC is a component in the calculation of Economic Profit (see page 26). Capital attribution strengthens risk management discipline. EC is calculated for the following eight distinct risk types: credit risk, goodwill and intangibles risk, operational risk, business risk, non-trading market risk, insurance risk, fixed asset risk and trading market risk. Credit, market insurance and operational risk are further detailed in the following sections. Business risk is the risk of loss due to variances in volumes, prices and costs caused by competitive forces, regulatory changes, and reputational and strategic risks. Goodwill and intangibles and fixed asset risks are defined as the risk that the value of these assets will be less than their net book value at a future date.

The combination of risk factors between and within risk categories and lines of business leads to some risk reduction, called diversification. These diversification benefits are passed on to our businesses. Therefore, Economic Profit and return on equity calculations are based on EC levels that include these diversification effects.

The following chart represents the proportionate EC levels by risk type for fiscal 2002.



The following sections discuss how we manage the major controllable risks including credit, market, liquidity, insurance and operational risk.

Credit risk

Credit risk is attributed to both on-balance sheet financial instruments such as loans and acceptances and credit equivalent amounts related to off-balance sheet financial instruments.

Our approach to credit risk management preserves the independence and integrity of risk assessment while being integrated into business management processes. Policies and procedures, which are communicated throughout the organization, guide the day-to-day management of credit risk exposure and are an essential part of our business culture. The goal of credit risk management is to evaluate and manage credit risk in order to further enhance this strong credit culture.

As discussed in the credit quality section on pages 45 to 52, we have significantly enhanced our loan mix. This improvement is being achieved through our strategy of reducing exposure to non-core corporate client relationships while increasing the size of the consumer portfolio, including residential mortgages, which have very low loss rates.

We are continually adding to and improving the analytical tools used to analyze, measure and manage credit risk. This includes the use of third-party modeling tools, increased use of stress testing and enhanced management information systems.

Risk ratings

Corporate borrowers are assigned an internal risk rating based on a detailed examination of the organization. This examination considers industry sector trends, market competitiveness, overall company strategy,

financial strength, access to funds, financial management and any other risks facing the organization. Our rating system is based on a 22-point scale.

Credit scoring models are utilized to determine a credit score for consumer and certain small business lending. The credit scores measure the relative risk of the initial extension of credit and any further increases. Consumer credit risk is monitored using statistical scoring models and payment history in order to predict portfolio behaviour.

The internal risk ratings and credit scores are assessed and updated on a regular basis.

Portfolio diversification

Portfolio diversification is our overriding principle, therefore, our credit policies and limits are structured to ensure we are not overexposed to any given client, industry sector or geographic area.

To avoid excessive losses if any particular counterparty is unable to fulfill its payment obligations, we have established single name limits that are set according to risk ratings. In certain cases loans are syndicated in order to reduce overall exposure to a single name.

Limits are also in place to manage exposure to any particular country or sector. Each country and sector is assigned a risk rating. This risk rating considers factors common to all entities in a given country or sector yet outside the control of any individual entity. Limits are determined based on the risk rating along with our overall risk appetite and business strategy.

Risk mitigation

In order to mitigate risk on portions of our portfolio we enter into credit derivative contracts. As at October 31, 2002, credit mitigation was in place to cover \$1.0 billion in corporate credit exposure. We also provided protection through credit derivatives to various counterparties totalling \$3.3 billion as at October 31, 2002.

Loan sales are also used to mitigate risk. We seek to identify and sell loans we have made to borrowers whose risk and reward profile and borrower ratings are no longer desirable to us.

In order to respond proactively to credit deterioration and mitigate risk, a problem loan workout group with specialized expertise handles the management and collection of nonaccrual loans as well as certain accrual loans.

Market risk

The level of market risk to which we are exposed varies continually, reflecting changing market conditions, expectations of future price and market movements and the composition of our trading and non-trading portfolios. We have established risk management policies and limits for our trading and asset/liability management activities that allow us to monitor and control the exposure to market risk resulting from these activities. We conduct trading activities over-the-counter and on exchanges in the spot, forward, futures and options markets and also participate in structured derivative transactions.

Interest rate risk

Interest rate risk is the potential adverse impact on our earnings and economic value due to changes in interest rates. In addition to the following discussion on trading activities please see the Non-trading portfolio section on page 61.

Credit spread risk

Credit spread risk is the potential adverse impact on our earnings and economic value due to changes in credit worthiness of persons we have credit exposure to both specifically and market-wide. We are exposed to credit spread risk through our holdings of bonds and credit derivatives. In the trading portfolio, credit spread risk arises from market-making activity as well as through proprietary trading in our credit derivatives trading unit.

Foreign exchange rate risk

Foreign exchange rate risk is the potential adverse impact on our earnings and economic value due to currency rate movements. We are exposed to foreign exchange rate risk in both the spot and forward foreign exchange markets and in the derivative market.

Equity risk

Equity risk is the potential adverse impact on our earnings due to movements in individual equity prices or general movements in the value of the stock market. We are exposed to equity risk from the buying and selling of equities as a principal in our brokerage business and our investment activities. Equity risk also results from our trading activities, including the providing of tailored equity derivative transactions to clients, arbitrage trading and proprietary trading.

Trading activities

Market risks associated with trading activities are a result of market-making, positioning and sales and arbitrage activities in the interest rate, foreign exchange and equity markets. Our trading operation primarily acts as a market-maker or jobber, executing transactions that meet the financial requirements of our clients and transferring the market risks to the broad financial market. We also act as principal and take market risk proprietary positions within the authorizations granted by our Board of Directors.

We recently completed a major upgrade of our enterprise market risk management system as part of our continuous renewal process to implement best practices and enhance our risk oversight capabilities. This represents a significant milestone in our ability to assess potential for loss using modeling techniques across all risk classes in a consistent and timely manner. In November 2002, we received regulatory approval to use an internal models approach for the regulatory capital requirement on specific risk of investment grade debt portfolios.

Value-At-Risk

Market risks associated with trading activities are managed primarily through the use of Value-At-Risk (VAR) methodology. VAR is a generally accepted risk measurement concept that uses statistical models and historical market price information to estimate within a given level of confidence the maximum loss in market value that we would experience in our trading portfolios from an adverse one-day movement in market rates and prices. Our VAR measure is based on a 99% confidence level and is an estimate of the maximum potential trading loss in 99 out of every 100 days. We use a historical simulation of the previous 500 trading day scenarios to determine VAR for our trading portfolio. The graph on page 56 shows the daily net trading revenue compared to the global trading VAR amounts for the year ended October 31, 2002. Net trading revenue is defined as the sum of the mark-to-market adjustments booked on trading positions and net interest income accrued from trading assets. During fiscal 2002, we experienced only four days of net trading losses, and we did not experience a single day with net trading losses in excess of the VAR estimate for that day.

Table 23 on the following page shows the year-end, high, average and low VAR by major risk category for our combined trading activities for the years ended October 31, 2002 and 2001. The table also shows our global VAR, which incorporates the effects of correlation in the movements of interest rates, exchange rates, equity prices and commodity prices and the resulting benefits of diversification within our trading portfolio. As the table illustrates, the average VAR in 2002 was \$11 million, the same as the average VAR in 2001. An increase in the interest rate VAR (due to the inclusion of credit spread risk within the VAR model) was offset by a reduction in risk within the equity trading portfolio.

TABLE 23 Market risk measures – Trading activities ⁽¹⁾

| (C\$ millions) | 2002 | | | | 2001 | | | |
|--|--------------|--------------|--------------|-------------|-------------|--------------|--------------|-------------|
| | Year-end | High | Average | Low | Year-end | High | Average | Low |
| Global VAR by major risk category | | | | | | | | |
| Equity | \$ 7 | \$ 12 | \$ 8 | \$ 6 | \$ 8 | \$ 16 | \$ 10 | \$ 6 |
| Foreign exchange and commodity | 2 | 9 | 3 | 1 | 2 | 6 | 3 | 1 |
| Interest rate | 11 | 14 | 6 | 2 | 3 | 9 | 4 | 2 |
| Global VAR ⁽²⁾ | \$ 13 | \$ 18 | \$ 11 | \$ 7 | \$ 8 | \$ 18 | \$ 11 | \$ 6 |

(1) Amounts are presented on a pre-tax basis and represent one-day VAR at a 99% confidence level.
(2) Global VAR reflects the correlation effect from each of the risk categories through diversification.

The Group Risk Management function, which is independent of the trading operations, is responsible for the daily measuring of global trading risk exposures. The function uses our VAR methodology to compare actual exposures to the limits established, to assess global risk-return trends and to alert senior management of adverse trends or positions. The function also develops and implements comprehensive risk measurement policies and risk limits that apply to trading activities.

We recognize that VAR is not an absolute measure of market risk and has its limitations since it is based on historical information only. In such circumstances, we implement other limits in order to control market liquidity risks, net position gap, term and volume for all products. This comprehensive market risk management framework is designed to ensure that an appropriate diversification of risks through policies is adopted on a global basis.

Back-testing

Back-testing against hypothetical profit and loss is used to monitor the statistical validity of VAR models. Hypothetical profit and loss is calculated by determining the impact of the actual one-day change in market rate or price movements on a given portfolio held constant for one day. Back-testing is performed daily across all trading portfolios. The results are submitted to OSFI on a quarterly basis. In fiscal 2002, there were two instances of the hypothetical net profit and loss exceeding the VAR. This is within the expected statistical range and supports the validity of the VAR model.

Stress testing

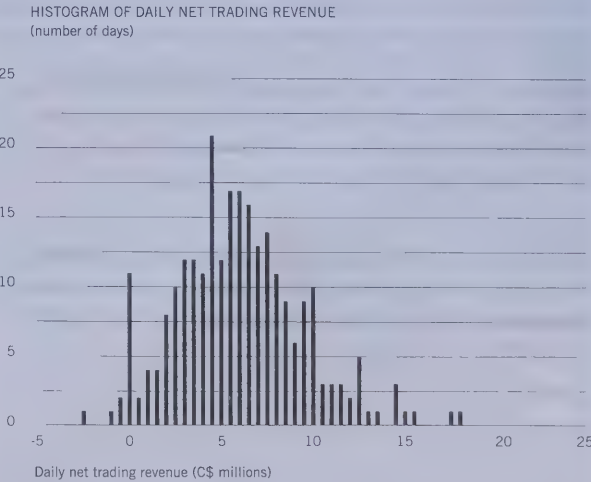
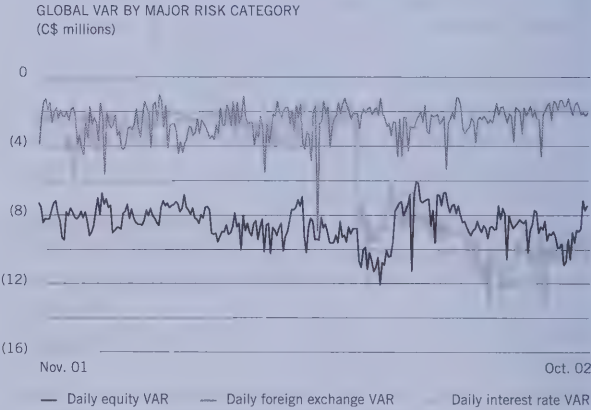
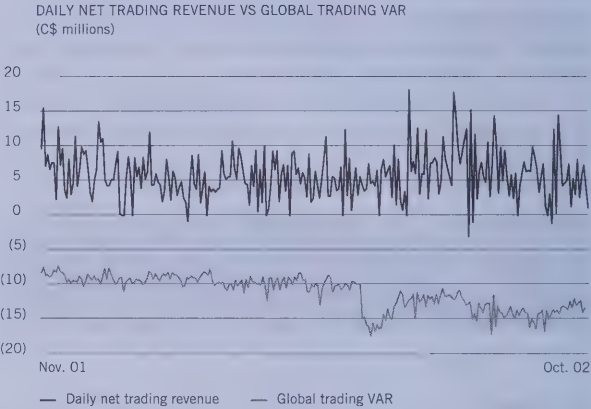
We also perform analysis on the potential trading losses due to stress events as a supplementary control on our market risk exposure. This is accomplished through applying historical and internally developed scenarios to the daily trading positions to monitor the effect of extreme market movements on the value of our portfolio.

Liquidity risk

The objective of liquidity management is to ensure we have the ability to generate or obtain sufficient cash or its equivalents on a timely and cost-effective basis to meet our commitments as they fall due. The management of liquidity risk is crucial to protecting our capital, maintaining market confidence and ensuring that we can expand into profitable business opportunities.

Liquidity risk is managed dynamically, exposures are continually measured, monitored and appropriately mitigated. We have developed and implemented a comprehensive liquidity management framework comprising policies, procedures, methodologies and measurements.

The Group Risk Committee and the Asset/Liability Committee provide guidance and oversight to our liquidity risk management program with the Audit Committee of the board approving our liquidity management framework and significant related policies. Corporate Treasury has global responsibility for developing liquidity management policies, strategies and contingency plans and for recommending and monitoring limits and coordinating subsidiary activities.



We have a Liquidity Crisis Team, composed of a cross-section of our senior executives. This team is responsible for the development, maintenance and success of our liquidity contingency plan. This plan would be activated in the event of a general market disruption or adverse economic developments that could destabilize our ability to meet obligations. This team meets regularly to review potential crisis scenarios and to update related action plans. Contingent liquidity exposures are identified and provisions are made to minimize possible damage through maintenance of a pool of unencumbered, high quality assets. These assets are marketable and can be immediately sold or pledged for secured borrowing and represent a dedicated and reliable source of emergency funding. In addition, a segregated portfolio of eligible securities is continuously available to support our participation in Canadian payment and settlement systems. For further information on liquidity see the Liquidity management section on page 62.

Insurance risk

Insurance risk includes product design and pricing risk, claims administration risk, underwriting risk and liability risk.

Product design and pricing risk

The process of designing and pricing products includes the estimation of many factors including future investment yields, mortality, morbidity, claims experience, expenses, policy lapse rates and taxes. Product design and pricing risk is the risk that actual experience will not match the assumptions made at the time pricing was determined and to the extent they differ, financial gains or losses will occur.

This risk is managed through detailed experience studies to support pricing assumptions and independent verification of scenario testing by our actuaries. In addition a portion of the policy benefit liabilities held on the balance sheet provides for misestimation and deterioration of assumptions from those assumed in the pricing. Risk is also mitigated through reinsurance, primarily for life insurance mortality and property and casualty catastrophe risks.

Claims administration risk

Claims administration risk is the exposure to higher than expected claims due to administrative practices in settling claims. Policies and procedures are in place that are designed to ensure that trained staff properly handle claims. There are approval limits in place to ensure that large dollar claims are handled and reviewed by experienced staff.

Underwriting risk

Underwriting risk is the exposure to financial losses resulting from the inappropriate selection and acceptance of the risks to be insured. Establishing policy retention limits that vary by market and geographic location mitigates exposure to large claims.

Liability risk

Liability risk exists when the attributes of a specific type of risk are misunderstood and improperly quantified and the liabilities established for this type of risk are inadequate. Actuaries review the assumptions used in the calculation of policy benefit liabilities on a quarterly basis.

Operational risk

Operational risk is the risk of direct or indirect loss resulting from inadequate or failed technology, human performance, processes or external events.

We endeavour to minimize operational losses by ensuring that effective infrastructure, controls, systems, and individuals are in-place throughout our organization. We employ dedicated professionals who are proactive in developing and implementing new methodologies for the identification, assessment and management of operational risk.

We have developed and are currently implementing two new processes aimed at monitoring and mitigating operational risks in the organization.

Risk and control self-assessment (RCSA)

RCSA is a formal process of proactively identifying, documenting, assessing and managing our operational risks. Each business segment and functional unit is divided into its component activities, which become entities to be assessed. Each entity completes a workshop-based, self-assessment to determine their key risks, mitigating controls, the potential impact and likelihood of a problem occurring and the acceptability of the residual risk after existing controls are considered.

Where residual risk is deemed unacceptable, the group will agree on an action plan and timeline. The findings of the various RCSAs conducted are documented, aggregated, analyzed and reported on a group-wide basis.

Loss event database (LED)

LED refers to a centralized database aimed at capturing information about operational losses. The losses tracked are mapped to the entities identified in the RCSA process.

Information such as the frequency, severity and nature of operational losses are captured. This data capture will allow analysis at the business segment and enterprise level. This will lead to a better understanding of the root causes of operational losses and improved risk mitigation strategies.

Ongoing development

Research and development efforts in the areas of quantification methodologies and key risk indicators will continue as we strive to stay at the forefront of risk management best practices.

Financial priority: Balance sheet and capital management

Highlights

- Consumer loans up 5%
- Deposits up 4%
- Internally generated capital of \$1.8 billion
- Capital ratios strengthened further
- Common share repurchases of \$764 million
- Redeemed US\$200 million of Series I and \$150 million of Series E preferred shares
- Redeemed \$400 million and issued US\$400 million of subordinated debentures

Total assets were \$382 billion at October 31, 2002, up \$19.5 billion or 5% from October 31, 2001.

Compared to October 31, 2001, securities were up \$14.3 billion or 18% and cash resources up \$3.8 billion or 22%. The growth in securities partially reflected higher levels of activity in our global equity derivatives business, which holds long and short positions in equity securities.

Total loans were up \$.4 billion or .2% from October 31, 2001, with the acquisition of Eagle Bancshares, in July 2002, contributing \$1.1 billion in loans and the acquisition of the private banking business of Barclays in June 2002, contributing \$.6 billion in loans. Consumer loans (residential mortgage, personal and credit card loans) were up \$5.5 billion or 5%. Residential mortgages were up \$5.4 billion or 8% (net of \$3.7 billion of mortgage securitizations during the year) and personal loans were down \$.5 billion or 2%. Credit card balances increased \$.6 billion or 15%, largely reflecting the maturity of \$.4 billion of credit card securitization term notes during the year. Business and government loans were down \$5.1 billion or 8%, largely reflecting planned reductions in the Canadian and U.S. corporate loan portfolios to enhance the quality of the business loan portfolio.

The \$1.0 billion increase in Other assets was largely driven by a \$2.6 billion increase in derivative-related amounts. This increase in derivative-related amounts was largely offset by a \$1.9 billion decrease in acceptances. Other – Other assets of \$13.5 billion includes \$805 million (US\$517 million) of receivables due from Cooperative Centrale Raiffeisen-Boerenleenbank B.A. (Rabobank), relating to a derivative contract that is the subject of litigation with Rabobank. While the outcome of any litigation cannot be predicted with certainty, we expect to recover this amount in its entirety and accordingly have not recorded any provision for loss (for further information see Note 18 on page 91).

Total deposits were \$245 billion, up \$9.4 billion or 4% from October 31, 2001. Interest-bearing deposits were up \$8.0 billion and non-interest-bearing deposits up \$1.4 billion. Personal deposits were up \$.5 billion, business and government deposits were up \$12.3 billion or 11% and bank deposits were down \$3.4 billion or 13%. Further details on deposits are provided in Note 10 on page 83.

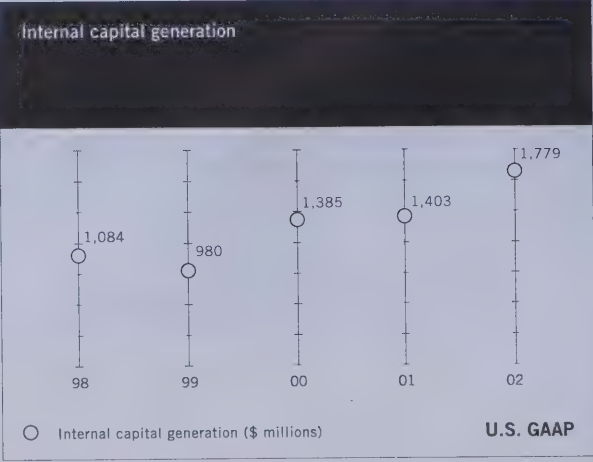
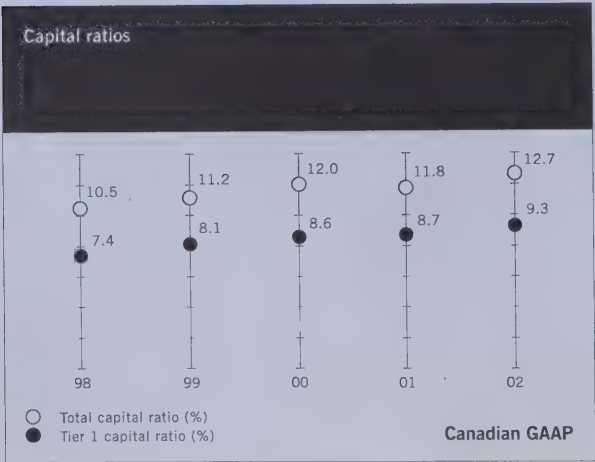
The fair value of loans and deposits differs from the respective book value due to changes in the levels of interest rates and changes in credit status. The estimated fair value of loans due from clients exceeded book values by \$2.2 billion at October 31, 2002 and \$4.4 billion at October 31, 2001. The estimated fair value of deposits owed to clients exceeded book values by \$1.5 billion at October 31, 2002 and \$2.4 billion at October 31, 2001. The net of the fair value excess of loans due from clients and the fair value excess of deposits due to clients was \$.8 billion at October 31, 2002, as shown in Note 21 on page 95. The estimated fair value of loans and deposits were in excess of book values largely due to a decline in interest rates.

RBC Capital Trust, a closed-end trust, has a total of \$1.4 billion of transferable trust units (RBC TruCS) outstanding. RBC TruCS are reported as non-controlling interest in subsidiaries on the consolidated balance sheet and are included in Tier 1 capital under guidelines issued by OSFI.

Total balance sheet capital, which includes shareholders' equity and subordinated debentures, was \$25.7 billion at October 31, 2002, up \$.6 billion or 3% from a year ago. The most significant factor behind the increase in capital over 2001 was internal capital generation of \$1.8 billion, partially offset by net capital redemptions and net share repurchases of \$.9 billion during 2002.

As required by Statement of Financial Accounting Standards, *Employers' Accounting for Pensions* (FAS 87), we recognized in Other comprehensive income an additional pension obligation of \$276 million, net of related income taxes. The increase in additional pension obligation is primarily due to the fair value of plan assets being less than the accumulated benefit obligation for certain plans this year. Asset values declined due to weak equity markets.

We fund the pension plans in accordance with regulatory requirements, which require funding when there is a deficit on a funding basis. Different assumptions and methods are prescribed for regulatory funding purposes versus accounting purposes. Our pension plans are in a surplus position for regulatory funding purposes. Note 15 on page 88 describes the funding position for accounting purposes.



Capital management

Capital management requires balancing the desire to maintain strong capital ratios and high debt ratings with the need to provide competitive returns to shareholders. In striving for this balance, we consider expected levels of risk-adjusted assets and balance sheet assets, future investment plans and the costs and terms of current and potential capital issues.

We are committed to maintaining strong capital ratios through internal capital generation, the issuance of capital instruments when appropriate, and controlled growth in risk-adjusted assets. We were able to achieve strong levels of internal capital generation despite weaker capital market conditions during the past year. The market environment and planned reductions of corporate loan exposures also contributed to slower growth in risk-adjusted assets, enabling us to continue repurchasing shares and redeeming some of our outstanding capital instruments. Our debt ratings continue to enhance our ability to raise capital at competitive prices.

Capital management activity

In fiscal 2002, we repurchased 14.3 million common shares, of which 4.5 million shares were repurchased for \$229 million under a normal course issuer bid that expired in June 2002, and 9.8 million shares were repurchased for \$513 million under a normal course issuer bid that allows for the repurchase of up to 20 million common shares, representing approximately 3% of outstanding common shares, between June 24, 2002 and June 23, 2003. During the fourth quarter of 2001, we entered into an agreement with an independent third party to execute an accelerated repurchase of six million common shares. This agreement resulted in an additional repurchase cost of \$22 million this year. In total, we spent \$764 million in connection with our share repurchases during 2002.

In November 2001, we redeemed US\$200 million of First Preferred Shares Series I and, in October 2002, redeemed \$150 million of First Preferred Shares Series E.

In November 2001, we issued US\$400 million of subordinated debentures through our European Medium Term Note Programme. In September 2002, we redeemed \$400 million of subordinated debentures.

Regulatory capital

Capital levels for Canadian banks are regulated pursuant to guidelines issued by OSFI, based on standards issued by the Bank for International Settlements (BIS). Regulatory capital is allocated into two tiers. Tier 1 capital comprises the more permanent components of capital. The components of Tier 1 and Tier 2 capital are shown in Table 24 below.

Regulatory capital ratios are calculated by dividing Tier 1 and Total capital by risk-adjusted assets based on Canadian GAAP financial information. Risk-adjusted assets, as shown in Table 25 on page 60, are determined by applying OSFI prescribed risk weights to balance sheet assets and off-balance sheet financial instruments according to the credit risk of the counterparty. Risk-adjusted assets also include an amount for the market risk exposure associated with our trading portfolio.

Our policy is to remain well capitalized so as to provide a safety net for the variety of risks to which we are exposed to in the conduct of our business. In 1999, OSFI formally established risk-based capital targets for deposit-taking institutions in Canada. These targets are a Tier 1 capital ratio of 7% and a Total capital ratio of 10%. As at October 31, 2002, our Tier 1 and Total capital ratios were 9.3% and 12.7%, respectively, compared to 8.7% and 11.8% at October 31, 2001. We maintained capital ratios that exceeded our medium-term goals of 8.0% for the Tier 1 ratio and 11–12% for the Total capital ratio. Effective November 1, 2002, we have raised our medium-term Tier 1 capital ratio goal to 8–8.5% from 8%. Our capital ratios on a U.S. basis, calculated using guidelines issued to U.S. banks by the Board of Governors of the Federal Reserve System and using U.S. GAAP financial information, are provided in Table 24 below.

Pending developments

In 1999, BIS issued a proposal for a new capital adequacy framework to replace the previous Capital Accord of 1988, under which we are currently regulated. This proposal continues to be at the discussion phase. Implementation of the final proposal is not likely to occur prior to fiscal 2006.

TABLE 24 Capital ratios (1)

| (C\$ millions, except percentage amounts) | 2002 | 2001 | 2000 |
|---|-------------------|-------------------|-------------------|
| Tier 1 capital | | | |
| Common equity | \$ 17,238 | \$ 16,141 | \$ 11,504 |
| Non-cumulative preferred shares | 1,545 | 2,024 | 2,037 |
| Non-controlling interest in subsidiaries | | | |
| RBC TruCS | 1,400 | 1,400 | 650 |
| Other | 29 | 28 | 23 |
| Goodwill | (4,832) | (4,742) | (647) |
| | 15,380 | 14,851 | 13,567 |
| Tier 2 capital | | | |
| Permanent subordinated debentures | 467 | 477 | 457 |
| Other subordinated debentures (2) | 6,147 | 5,935 | 5,138 |
| General allowance (3) | 1,420 | 1,410 | 1,188 |
| Non-controlling interest in subsidiaries | – | – | 1 |
| | 8,034 | 7,822 | 6,784 |
| Investment in insurance subsidiaries | (2,014) | (2,107) | (960) |
| Other substantial investments | (368) | (387) | (342) |
| First loss facility | (20) | (8) | (5) |
| Total capital | \$ 21,012 | \$ 20,171 | \$ 19,044 |
| Risk-adjusted assets | \$ 165,559 | \$ 171,047 | \$ 158,364 |
| Capital ratios (4) | | | |
| Common equity to risk-adjusted assets | 10.4% | 9.4% | 7.3% |
| Tier 1 capital to risk-adjusted assets | 9.3% | 8.7% | 8.6% |
| Total capital to risk-adjusted assets | 12.7% | 11.8% | 12.0% |
| Assets-to-capital multiple (5) | 17.3 | 17.2 | 15.3 |
| U.S. basis (4), (6) | | | |
| Tier 1 capital to risk-adjusted assets | 8.5% | 8.1% | 7.8% |
| Total capital to risk-adjusted assets | 11.9% | 11.2% | 11.3% |
| Equity to assets (7) | 4.9% | 5.3% | 4.5% |

(1) Using guidelines issued by the Superintendent of Financial Institutions Canada and Canadian GAAP financial information except as noted in footnote (6).

(2) Subordinated debentures that are within five years of maturity are subject to straight-line amortization to zero during their remaining term and, accordingly, are included above at their amortized value.

(3) The general allowance for credit losses may be included in Tier 2 capital up to a maximum of .875% (2001 – .875%; 2000 – .75%) of risk-adjusted assets.

(4) On November 26, 2001, we redeemed US\$200 million of Non-cumulative First Preferred Shares Series I, which reduced Tier 1 capital by the same amount. On November 8, 2001, we issued US\$400 million of subordinated debentures, which increased Total capital by the same amount. Had these transactions taken place as at October 31, 2001, the 2001 pro forma capital ratios would have been: Tier 1 capital ratio – 8.5% and Total capital ratio – 12.0%. Using guidelines issued by the Board of Governors of the Federal Reserve System in the United States and U.S. GAAP financial information, the pro forma U.S. basis capital ratios would have been Tier 1 capital ratio – 7.9% and Total capital ratio – 11.4%.

(5) Total assets and specified off-balance sheet financial instruments, as prescribed by the Superintendent of Financial Institutions Canada, divided by Total capital.

(6) Using guidelines issued by the Board of Governors of the Federal Reserve System in the United States and U.S. GAAP financial information.

(7) Average total shareholders' equity divided by average total assets.

- (1) Using guidelines issued by the Superintendent of Financial Institutions Canada and Canadian GAAP financial information.
- (2) Represents the weighted average of counterparty risk weights within a particular category.
- (3) Amounts are shown net of allowance for loan losses.
- (4) Represents the total current replacement value of all outstanding contracts in a gain position, before factoring in the impact of master netting agreements. Exchange-traded instruments are subject to daily margin requirements. Such instruments are excluded from the calculation of risk-adjusted assets as they are deemed to have no additional credit risk. The fair value of \$194 million (2001 - \$194 million) is excluded at October 31, 2002. Written options are excluded as they represent our obligations and as such do not attract credit risk.
- (5) Consists of (i) the total positive replacement value of all outstanding contracts, and (ii) an amount for potential future credit exposure.
- (6) The notional amount of \$5,593 million (2001 - \$1,693 million) and replacement cost of \$93 million (2001 - \$49 million) of derivatives embedded in financial instruments, certain warrants and loan commitments considered as derivatives are excluded from the amounts in this table.
- (7) Comprises default swaps, total return swaps and credit default baskets.
- (8) Comprises precious metals, commodity and equity-linked derivative contracts.

Asset/liability management

Overview

Asset/liability management comprises the evaluation, monitoring and management of our non-trading portfolio, liquidity management and funding. It is important to note that liquidity and capital resources are likely to be affected by many of the same factors which are detailed in this section of Management's discussion and analysis, the Factors discussion on pages 23 to 24 and the Risk management discussion on pages 53 to 57. Additionally, off-balance sheet financing arrangements are often integral to both liquidity and capital resources, and are discussed in detail on pages 64 to 65 of this section.

Non-trading portfolio

Traditional banking activities, such as deposit taking and lending, expose us to market risk, of which interest rate risk, as described on page 55, is the largest component.

We actively manage the interest rate risk for the North American non-trading balance sheet and oversee all other non-trading units that have been delegated interest rate risk limits. We endeavour to adopt industry best practices and carry out the following functions:

Policy

The Conduct Review and Risk Policy Committee of the Board of Directors approves the global policies governing interest rate risk management. The policies define the acceptable limits within which risks to net interest income over a 12-month horizon and the economic value of equity are to be managed. These ranges are based on immediate and sustained \pm 200 basis points parallel shifts of the yield curve. The limit for net interest income risk is 6% of projected net interest income and for economic value of equity risk is 12% of projected common equity.

Interest rate funds transfer pricing

We use a funds transfer pricing mechanism to centralize interest rate risk within Corporate Treasury and to ensure an economic allocation of interest income to the various business units. Funds transfer pricing at the transaction level ensures that interest rate risk is appropriately transferred to Corporate Treasury for management. The funds transfer pricing rates are market-based and aligned with risk management principles. They are supported by empirical research into client behaviour and are an integral input to the retail business pricing decisions.

Applied research

We are dedicated to investigating best practices in instrument valuation, econometric modeling and new hedging techniques. These investigations range from evaluation of traditional asset/liability management processes to application of recent developments in quantitative methods to our processes.

We focus on developing retail product valuation models that incorporate consumer behaviour. These valuation models are typically derived through econometric estimation of consumer exercise of options embedded in retail products. The most significant embedded options are mortgage rate commitments and prepayment options. On the liability side of the balance sheet, we tend to focus on modeling administered rates and the sensitivity of liability balances to interest rate changes.

Risk measurement

We continue to make significant investment in new technology to facilitate measurement and timely management of our interest rate risk position. A range of static and dynamic scenarios is used every week to measure our risk position based on client rates as well as funds transfer pricing rates.

Static scenarios allow us to analyze our risk at a particular point in time under various interest rate assumptions. These assumptions comprise parallel shocks as well as twists to the current yield curve. Static scenarios are employed for assessing the economic value of equity risk as well as the net interest income risk. Dynamic scenarios simulate our interest income in response to various combinations of business and market factors. Business factors include assumptions about future pricing strategies and volume and mix of new business, whereas market factors include assumptions such as changes in interest rate levels and changes in the shapes of yield curves.

We measure our risk positions for the Canadian non-trading balance sheet every week and are capable of identifying the various sources of interest rate risk.

Interest rate risk management

Our goal is to manage interest rate risk of the non-trading balance sheet to a targeted level, on a continual basis. We modify the risk profile of the balance sheet through proactive hedging activity.

The interest rate risk can be disaggregated into linear risk and non-linear risk based on the varying responses of the balance sheet to different interest rate movements. The linear risk is primarily managed through interest rate swaps. The non-linear risk arises mainly from embedded options in our products that allow clients to modify the maturities of their loans or deposits. Examples are a client pre-paying a personal loan or a prospective client getting a committed rate on a new mortgage before the mortgage loan takes effect. Embedded options are modeled using assumptions based on empirical research and are managed by either purchasing options or by a dynamic hedging strategy.

The performance of interest rate risk management function within Corporate Treasury is benchmarked on a total return basis. A by-product of this benchmarking exercise is a methodology that controls model risk by continuously back-testing model assumptions against actual client behaviour.

Table 26 below presents the potential impacts of 100 and 200 basis point increases and decreases in interest rates on our economic value of equity and on current earnings on our non-trading portfolio. These measures are as of October 31, 2002, and are based on assumptions made by management and validated by empirical research. The methodology assumes that no further hedging is undertaken. We have defined a risk neutral balance sheet as one where net residual assets representing equity are evenly invested over a five-year horizon. As a result of this decision, our interest rate risk profile has slightly faster re-pricing of assets than of liabilities with the duration of equity at about 2.5 years.

All interest rate measures in this section are based upon our interest rate exposures at a specific time. The exposures change continually as a result of day-to-day business activities and our risk management initiatives.

| TABLE 26 Market risk measures – Non-trading activities ⁽¹⁾ | | | | |
|--|-------------------------------|--------------------------|-------------------------------|--------------------------|
| (C\$ millions) | 2002 | | 2001 | |
| | Economic value of equity risk | Net interest income risk | Economic value of equity risk | Net interest income risk |
| 100bp increase | \$ (309) | \$ 104 | \$ (390) | \$ 96 |
| 100bp decrease | 145 | (151) | 256 | (108) |
| 200bp increase | \$ (662) | \$ 190 | \$ (842) | \$ 179 |
| 200bp decrease | 345 | (327) | 466 | (294) |

(1) Amounts are presented on a pre-tax basis as at October 31.

Liquidity management

Our liquidity management framework is designed to ensure that reliable and cost-effective sources of cash are available to satisfy current and prospective commitments, both on and off-balance sheet. The primary goals of this framework are the preservation of a large base of core client deposits, ongoing access to diversified sources of wholesale funding and the maintenance of a dedicated pool of unencumbered marketable securities that provide ready access to cash.

The Corporate Treasury function has global responsibility for the development of liquidity management policies, strategies and contingency plans and for recommending and monitoring limits within this framework. Our principal regional trading and funding platforms provide transactional support for liquidity management policies and strategies. The Group Risk Management Committee and the Asset/Liability Committee share management oversight of liquidity management and receive regular reports detailing compliance with limits and guidelines. The Audit Committee of the Board of Directors approves our liquidity management framework and significant related policies and is informed on a periodic basis about our current and prospective liquidity condition. Additionally, we have a liquidity contingency plan in place, which is maintained and administered by the Liquidity Crisis Team. Subsidiaries are responsible for managing their own liquidity in compliance with policies, practices and governing regulatory requirements.

We measure and monitor our liquidity condition from structural, tactical and contingent perspectives. The assessment of our liquidity position based on these measures reflects management estimates and judgments pertaining to the behaviour of our clients and future market conditions.

Structural liquidity risk management

Existing balance sheet composition can create liquidity exposure due to mismatches in effective maturities between assets and liabilities. Structural liquidity risk management addresses this type of exposure, which is measured and monitored through ongoing stress testing of our balance sheet.

We recently adopted the cash capital model to assist in the evaluation of balance sheet liquidity and in the determination of the appropriate term structure of our debt financing. This methodology provides a comprehensive, formula-based approach for the assessment of balance sheet integrity and our ability to continue as a going concern during a prolonged liquidity event, such as an unexpected withdrawal of short-term funding. The application of this model entails assigning liquidity discounts or "haircuts" to our balance sheet assets based on our assessment of the cash-generating characteristics of each asset category in the context of a sustainable business model. The illiquid component of our balance sheet assets can be determined by this analysis. Liabilities are arrayed along a stability continuum, ranging from core to volatile, on the basis of both contractual and behavioural properties in order to identify the constant elements of our funding. This analysis of our balance sheet enables us to more accurately estimate our exposure to a protracted loss of unsecured funding and to quantify our longer-term financing requirements.

Tactical liquidity risk management

Tactical liquidity risk management addresses our normal day-to-day funding requirements and is managed by imposing limits on net funds outflows for specified periods, particularly for key short-term time horizons. Scenario analysis is performed periodically on the assumed behaviour of cash flows under varying conditions to assess funding requirements and, as required, to update assumptions and limits. Detailed reports on our principal short-term asset/liability mismatches are monitored on a daily basis to ensure compliance with the prudential limits established for overall group exposure and by major currency and geographic location. Corporate Treasury issues procedural directives to the individual units engaged in executing policy to ensure consistent application of cash flow management principles across the entire organization.

Contingent liquidity risk management

The liquidity contingency plan identifies comprehensive action plans that would be implemented in the event of general market disruptions or adverse economic developments that could jeopardize our ability to meet commitments. Four different market scenarios, of varying duration and severity, are addressed in the liquidity contingency plan to highlight potential liquidity exposures and requisite responses. The Liquidity Crisis Team, comprising senior individuals from business and functional units, meets regularly to review and update implementation plans and to consider the need for activation in view of developments in Canada and globally.

To address potential liquidity exposures identified by our scenario analyses, we maintain a pool of segregated and unencumbered marketable securities. These high-quality assets can be readily sold or pledged for secured borrowing and represent a dedicated and reliable source of emergency funding. In addition, we maintain a separate portfolio of eligible assets to support our participation in Canadian payment and settlement systems. Liquid assets and assets purchased under reverse repurchase agreements (before pledging as detailed below) totalled \$155 billion or 41% of total assets at October 31, 2002 as compared to \$137 billion or 38% respectively at October 31, 2001. Canadian dollar liquid assets are primarily marketable securities while a material portion of our foreign currency liquid assets are issued by highly rated foreign banks. As at October 31, 2002, \$10 billion of assets had been pledged as collateral, up from \$9 billion at October 31, 2001. We have another \$39 billion in obligations related to assets sold under repurchase agreements or securities sold short at October 31, 2002, compared to \$37 billion at October 31, 2001. For further details, see Note 18 on page 92.

Funding strategy

Diversification of funding sources is a crucial component of our overall liquidity management strategy since it expands funding flexibility, minimizes funding concentration and dependency and generally lowers financing costs. Core funding, comprising capital, longer-term liabilities and a diversified pool of personal and, to a lesser extent, commercial deposits, is the foundation of our strong structural liquidity position.

Credit ratings

Our ability to access unsecured funding markets and our financing costs in such markets are primarily dependent upon maintaining acceptable credit ratings, which in turn is largely determined by the quality of our earnings, the adequacy of our capital and the effectiveness of our risk management programs. While our estimates suggest that a minor downgrade would not materially influence our funding capacity or costs, we recognize the importance of avoiding such an event and are committed to actions that should reinforce existing external assessments of the bank's financial strength. A series of downgrades could have an adverse impact on our funding capacity and on the results of our operations.

Deposit profile

Personal deposits remain the prime source of funding for our Canadian dollar balance sheet while most foreign currency deposits originate from unsecured, "wholesale" sources, including large corporate and institutional clients and foreign commercial and central banks. Our personal deposit franchise constitutes a principal source of predictable and dependable funding. Certain commercial and institutional client groups also maintain relational balances with relatively low volatility profiles, a portion of which are considered core funding for structural liquidity purposes. Relational balances are typically maintained by commercial and corporate clients to facilitate their daily operating requirements. In some businesses, collective balances are substantial and exhibit a high degree of relative stability. We promote wholesale funding diversity and regularly review sources of short-term funds to ensure maintenance of wide

diversification by provider, product and geographic origin. In addition, we maintain an ongoing presence in different funding markets, constantly monitoring market developments and trends in order to identify opportunities or risks and to take appropriate pre-emptive actions. For further details see Note 10 on page 83.

Term funding sources

Long-term funding strategy is integrated with our current and estimated structural liquidity position as reflected in our cash capital position. Liquidity objectives, as well as market conditions, interest rates, credit spreads and desired financial structure, influence annual long-term funding activities, including currency mix and market concentration. Diversification into new markets and untapped investor segments is constantly evaluated against relative issuance costs. Our long-term funding sources are managed to minimize concentration by geographic location, investor segment, and currency and maturity profile. During fiscal 2002, we continued to expand our long-term funding base by issuing \$2.6 billion of senior deposit notes in various currencies and markets. Total unsecured long-term funding outstanding at October 31, 2002 was \$13.2 billion, compared with \$12.6 billion at October 31, 2001.

We use asset securitization programs as an alternative source of funding, to provide liquidity and for asset/liability management purposes. In particular, \$1.7 billion in new financing was provided during the year by the securitization and sale of government guaranteed residential mortgages (MBS). Our total outstanding MBS sold at year-end was \$2.4 billion. In addition, \$1.7 billion of our credit card receivables have been securitized through notes issued by a securitization SPE (see page 64, Special purpose entities – securitization for more details).

Off-balance sheet

In the normal course of business, we engage in a variety of financial transactions that, under GAAP, are either not recorded on our balance sheet or are recorded on our balance sheet in amounts that differ from the full contract or notional amounts. These transactions involve, among other risks, varying degrees of market, credit and liquidity risk, which are discussed in the Risk management section on pages 53 to 57. Off-balance sheet transactions are either proprietary or client transactions, and are generally undertaken for risk management, capital management and/or funding management purposes. The types of off-balance sheet activities we undertake include issuance of credit instruments and lease commitments, derivative financial instruments and transactions with SPEs. Each of these types of activities is discussed below.

Credit instruments

We provide credit instruments to our clients to help them meet their financing needs. Guarantees and standby letters of credit carry the same credit risk as loans and represent irrevocable assurances that we will make payments in the event that a client cannot meet its obligations to

third parties. On behalf of clients, we also undertake written documentary and commercial letters of credit, authorizing a third party to draw drafts from us to a stipulated amount and typically having underlying shipments of goods as collateral. We make commitments to extend credit, which may represent unused portions of authorizations to extend credit in the form of loans, acceptances, guarantees and letters of credit. We have uncommitted amounts, which represent revocable offers by us to extend credit to a borrower, but not obligations to extend credit. We are also party to note issuance facilities (including revolving facilities), which represent underwriting agreements that enable a borrower to issue short-term debt securities. Table 27 below provides a detailed summary of our off-balance sheet credit instruments.

Lease commitments

We have made minimum future rental commitments for premises and equipment under long-term non-cancellable leases, which are detailed for each of the next five years and thereafter in Table 27 below. Our lease agreements do not contain any covenants that restrict our ability to pay dividends, engage in debt or equity financing transactions, or enter into additional lease agreements.

Derivative financial instruments

As a part of our institutional sales and trading activities, we act as counterparty to clients in transactions involving derivative financial instruments. We undertake this role to assist our clients in managing their exposure to various types of risk. We also engage in transactions involving derivative financial instruments with other counterparties to manage our exposure to interest rate, currency, credit and market risks (market risks are discussed on page 55). All derivatives are recorded at fair value on our balance sheet (fair value assumptions are discussed on page 25). Although derivative transactions are measured in terms of their notional amounts, these amounts are not recorded on our balance sheet, as the notional amounts serve as points of reference for calculating payments, and are not the actual amounts that are exchanged. Table 25 on page 60 details the notional amount, credit equivalent amount and risk-adjusted balances by derivative contract type. Note 19 on pages 93 and 94, details the notional amount of derivatives by reference to term to maturity and replacement cost, respectively.

To the extent that one or more of the derivative financial transactions we undertake involve amounts owing from third-party counterparties, we are exposed to counterparty credit risk (credit risk is discussed in more detail on page 54). Total credit risk as represented by the fair value of all derivatives that have a positive market value amounted to \$10.6 billion as at October 31, 2002, and is recorded at replacement cost on our balance sheet. Additionally, Notes 1 and 19 on pages 73 to 74 and 92 to 94, respectively, provide more detail on the accounting for derivatives.

TABLE 27 Lease commitments and credit instruments

| (C\$ millions) | Within 1 year | 1 to 3 years | Over 3 to 5 years | Over 5 years | Total |
|--|---------------|--------------|-------------------|--------------|------------|
| Lease commitments | \$ 364 | \$ 630 | \$ 470 | \$ 754 | \$ 2,218 |
| Credit instruments | | | | | |
| Guarantees and standby letters of credit | 4,159 | 6,247 | 1,526 | 1,678 | 13,610 |
| Documentary and commercial letters of credit | 378 | 236 | 118 | 40 | 772 |
| Commitments to extend credit | 44,832 | 10,624 | 4,233 | 15,357 | 75,046 |
| Uncommitted amounts | 814 | 41,121 | 2,835 | 1,208 | 45,978 |
| | 50,183 | 58,228 | 8,712 | 18,283 | 135,406 |
| Total | \$ 50,547 | \$ 58,858 | \$ 9,182 | \$ 19,037 | \$ 137,624 |

Special purpose entities

Special purpose entities (SPEs) are principally used to securitize financial and other assets in order to obtain access to funding, to mitigate credit risk and to manage capital. SPEs are an important part of the financial markets, providing market liquidity by facilitating investors' access to specific portfolios of assets and risks in a form that meets their investment criteria. We use SPEs to securitize a portion of our credit card receivables. We provide SPE repackaging services to clients who seek access to financial assets in a form different than what is conventionally available. We also act as an intermediary or agent for clients who want to use SPEs to securitize their own financial assets.

SPEs are typically set up for a single, discrete purpose, have a limited life and serve to legally isolate the financial assets held by the SPE from the selling organization. SPEs are not operating entities and usually have no employees. The typical SPE structure involves a company selling assets to the SPE. The SPE funds the purchase of those assets by issuing securities to investors in the form of certificates, commercial paper or other notes of indebtedness. The financial interests of investors in SPEs are usually limited to interests in the assets of the SPE, and to various forms of credit enhancement accompanying the SPE assets, which may include conditional access to a cash collateral account, over-collateralization in the form of excess assets in the SPE or a line of credit facility. Liquidity and credit facilities as well as interest rate and other swaps may be provided by financial institutions to address mismatches between the cash flows of the underlying assets and the indebtedness issued by the SPE.

We provide services to SPEs in a number of different capacities including administration of the SPEs and the underlying asset pools, as a trustee for SPEs' assets, as a liquidity or credit enhancement provider, or as a counterparty in transactions involving derivative financial instruments or as collateral manager.

We manage and monitor our direct involvement with SPEs through our SPE Risk Committee, which is comprised of representatives from functional areas including risk management, corporate treasury, finance, subsidiary governance office, law, taxation, subsidiary banking groups and human resources. This committee's key activities include formulating policies governing SPEs, reviewing new and unusual SPE transactions and monitoring the ongoing activities of SPEs.

The Financial Accounting Standards Board is currently drafting new accounting standards on the consolidation of SPEs. Since these new standards are still being drafted their impact on our balance sheet is not quantifiable but could result in us consolidating certain assets and liabilities held in our SPEs.

Securitization of credit card receivables

We securitize some of our credit card receivables through an SPE. The SPE is funded through the issuance of senior and subordinated notes collateralized by the underlying credit card receivables. The primary economic purpose of this activity is to diversify our sources of funding and to enhance our liquidity position. Although these credit card receivables are no longer on our balance sheet, we maintain the client account and retain the relationship.

The transfer of the credit card receivables to the custodian of those assets is a sale from a legal perspective. In addition, our credit card securitization structure qualifies for sale treatment from an accounting perspective. Under FAS 140, the receivables are removed from our balance sheet resulting in a gain or loss reported in non-interest revenue. Note 7 on pages 81 and 82 provides information on our key securitization activities, including key assumptions. This SPE meets the Statement

of Financial Accounting Standard, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* (FAS 140) criteria for a Qualifying SPE (QSPE) and, accordingly, as the transferor of the credit card receivables, we are precluded from consolidating this SPE.

We continue to service the credit card receivables sold to the QSPE. In addition, we perform an administrative role for the QSPE in which we are responsible for ensuring that the ongoing public filings of the QSPE are performed, as required, and that the investors in the QSPE's asset-backed securities receive interest and principal payments on a timely basis.

We provide first loss protection to the QSPE in two forms. Our interest in the excess spread from the QSPE is subordinate to the QSPE's obligation to the holders of its asset-backed securities. Excess spread is the residual net interest income after all other trust expenses have been paid. Therefore, our excess spread serves to absorb losses with respect to the credit card receivables before payments to the QSPE's noteholders are affected. The present value of this excess spread is reported as a retained interest within available for sale securities on our consolidated balance sheet. In addition, we provide loans to the QSPE to pay up-front expenses. These loans rank subordinate to all notes issued by the QSPE.

At October 31, 2002, total credit card receivables securitized and held off-balance sheet amounted to \$1.7 billion, compared to \$2.1 billion at October 31, 2001. The carrying value of our retained interests in securitized credit card receivables at October 31, 2002, was \$15.1 million compared to \$19.5 million in 2001, and amounts receivable under subordinated loan agreements were \$5.2 million compared to \$8.5 million in 2001.

Securitization of client financial assets

Within our global securitization group, our principal relationship with SPEs comes in the form of administering multi-seller asset-backed commercial paper conduit programs (multi-seller SPEs). We currently administer five multi-seller SPEs – three in Canada and two in the U.S. These five multi-seller SPEs have purchased financial assets from our clients totalling \$20.6 billion. Under current accounting standards, the five multi-seller SPEs that we administer are not consolidated on our balance sheet.

We are involved in the multi-seller SPE markets because our clients value these transactions, they offer a growing source of revenue and they generate a favorable risk-adjusted return for us. Our clients primarily utilize multi-seller SPEs to diversify their financing sources and to reduce funding costs by leveraging the value of high quality collateral.

The multi-seller SPEs purchase various financial assets from clients and finances those purchases by issuing highly rated asset-backed commercial paper. The multi-seller SPEs typically purchase the financial assets as part of a securitization transaction by our clients. In these situations, the sellers of the financial assets continue to service the respective assets and generally provide some amount of first-loss protection on the assets. We do not maintain any ownership or retained interest in these multi-seller SPEs. Instead, we provide or retain certain services such as transaction structuring and administration as specified by the multi-seller SPE's program documents and based on rating agency criteria. In addition, we provide backstop liquidity facilities and partial credit enhancement to the multi-seller SPEs. We receive market-based fee revenue from such services, which is reported as non-interest revenue. We also have no rights to, or control of, the assets owned by the multi-seller SPE.

The table below summarizes the financial assets owned by the originator and sold to the trust or trust-like structure (trust-seller SPEs) and the trust or trust-like structure (trust-buyer SPEs) at fiscal years ended October 31.

| Asset class | | |
|-------------------------------|------------------|------------------|
| (C\$ millions) | 2002 | 2001 |
| Credit cards | \$ 4,671 | \$ 3,785 |
| Auto loans and leases | 3,615 | 4,298 |
| Equipment receivables | 2,509 | 2,159 |
| Trade receivables | 2,479 | 2,094 |
| Residential mortgages | 2,004 | 1,682 |
| Other loans | 1,275 | 843 |
| Dealer floor plan receivables | 1,208 | 1,275 |
| Consumer loans | 1,196 | 1,114 |
| Asset-backed securities | 926 | 487 |
| Other | 706 | 579 |
| | \$ 20,589 | \$ 18,316 |

The commercial paper issued by each multi-seller SPE is in the SPE's own name with recourse to the financial assets owned by the multi-seller SPE. The multi-seller SPE commercial paper is non-recourse to us and non-recourse to the other multi-seller SPEs that we administer. Each multi-seller SPE is largely prohibited from issuing medium-term notes or other forms of indebtedness to finance the asset purchases. Consequently, each multi-seller SPE's commercial paper liabilities are generally equal to the assets owned by that multi-seller SPE. The small difference between each of the multi-seller SPE's assets and liabilities balances is mostly related to the discount or interest costs attributable to the commercial paper. As of October 31, 2002, the total face amount of commercial paper issued by the multi-seller SPE's equaled \$20,589 million generating \$20,534 million of cash proceeds with the difference between these amounts representing the commercial paper discount.

At fiscal years ended October 31, total commitments and amounts outstanding under liquidity and credit facilities were as shown in the following table:

Liquidity and credit facilities

| | 2002 | | 2001 | |
|----------------------|-----------|-------------|-----------|-------------|
| (C\$ millions) | Committed | Outstanding | Committed | Outstanding |
| Liquidity facilities | \$ 22,593 | \$ — | \$ 20,614 | \$ — |
| Credit facilities | 7,211 | — | 3,856 | — |
| | \$ 29,804 | \$ — | \$ 24,470 | \$ — |

We provide backstop liquidity facilities to the multi-seller SPEs as an alternative source of financing in the event that such SPEs are unable to access commercial paper markets, or in limited circumstances, when pre-determined performance measures of the financial assets owned by the multi-seller SPEs are not met. The terms of the backstop liquidity facilities do not require us to advance money to the multi-seller SPEs in the event of bankruptcy or to purchase non-performing or defaulted assets. None of the backstop liquidity facilities that we have provided has ever been drawn upon.

The partial credit enhancement that we provide to the multi-seller SPEs is in place to protect commercial paper investors in the event that the credit enhancement supporting the asset pools proves to be insufficient to prevent a default of one or more of the asset pools. Each of the asset pools is structured to achieve a high investment grade credit profile through credit enhancement related to each transaction. As a result, we believe that the program credit enhancements that we provide to the multi-seller SPEs present a modest amount of credit risk.

The economic exposure that we assume when we provide backstop liquidity commitments and partial credit enhancement is contingent in nature. We manage these exposures within our risk management functions in the same manner that we manage other contingent and non-contingent risk exposures. Our risk management process considers the credit, liquidity and interest rate exposure related to each of the assets. The risk exposure of each of these components individually and taken as a whole is deemed to be acceptable. All transactions are reviewed by external rating agencies. The weighted average credit quality of the assets supported by our backstop liquidity and partial credit enhancement is among the highest quality rating levels based on our internal risk rating system, which is described on page 54. The liquidity risk to us is deemed to be low based on the historical performance and high credit quality of the multi-seller SPEs' assets. Interest rate exposure is deemed to be low and is generally managed at the transaction level by passing on the funding cost variability to the securitization structures. Corporate Treasury scrutinizes contingent balance sheet risk, in effect monitoring the risk of drawdown under any of the credit facilities.

Creation of investment products

We use repackaging SPEs to create unique credit products to meet the needs of investors with specific requirements. As part of this process, we may enter into derivative contracts with these SPEs in order to convert various risk factors such as yield, currency or credit risk of underlying assets to meet the needs of our clients. In this role as derivative counterparty to the SPE, we assume the associated counterparty credit risk of the SPE. In order to enter into these transactions we establish an internal risk rating of the SPE and provide ongoing risk assessment and monitoring of the SPE's credit risk. As with all counterparty credit exposures, these exposures are put in place and reviewed pursuant to our normal risk management process in order to effectively manage and monitor this credit risk profile.

These SPEs often issue notes. Those notes may also be rated by external rating agencies, as well as listed on a stock exchange and are generally traded via recognized bond clearing systems. While the majority of the notes that are created in repackagings are expected to be sold on a 'buy & hold' basis, we may on occasion act as market-maker. We do not, however, provide any repackaging SPE with any guarantees or other similar support commitments. There are many functions required to create a repackaged product. We fulfill some of these functions and independent third parties or specialist service providers fulfill the remainder. Currently we act as sole arranger and swap provider for SPEs where we are involved, and in most cases as paying and issuing agent as well.

Asset management

We act as collateral manager for several collateralized debt obligation (CDO) SPEs, which invest in leveraged bank-initiated term loans, high-yield bonds and mezzanine corporate debt. As collateral manager, we are engaged by the CDO SPE, pursuant to a Collateral Management Agreement, to advise the SPE on the purchase and sale of collateral assets it holds. For these advisory services, we are paid a pre-determined market-based fee, which is a percentage of assets held by the SPE.

The notional amount of the CDOs we managed at the end of fiscal 2002 was US\$1.6 billion (2001 – US\$1.3 billion). Although we have a nominal investment of US\$9.5 million in the “first-loss” tranche of a US\$300 million CDO, we provide no liquidity or credit support to these SPEs beyond this investment. The CDOs we manage may from time-to-time purchase collateral assets originated by us or other affiliates. The program documents covering the formation and operation of the individual CDOs provide strict guidelines for the purchase of such assets.

We recognize fee income from collateral management services and, where indicated, interest income from investments in individual CDOs.

2001 compared to 2000

The following discussion and analysis provides a comparison of our results of operations for the years ended October 31, 2001 and 2000. This discussion should be read in conjunction with the consolidated financial statements and related Notes on pages 67 to 96. This portion of the management's discussion and analysis is based on amounts reported in the consolidated financial statements and does not exclude special items.

Business segment results

Net income from RBC Banking increased 10% to \$1,174 million in 2001 from \$1,064 million in 2000. ROE decreased 270 basis points to 16.8%.

Net income from RBC Insurance was up 68% to \$173 million in 2001, reflecting acquisitions. ROE decreased from 38.6% to 20.0% due to higher allocation of capital in light of recent acquisitions.

Net income from RBC Investments was up 23% from 2000 to \$508 million. ROE declined by 2,080 basis points to 27.0% due to higher allocation of capital as a result of recent acquisitions.

Net income from RBC Capital Markets decreased 30% to \$349 million, reflecting a large increase in the provision for credit losses. ROE declined by 1,120 basis points to 9.6%, reflecting lower net income and the higher allocation of capital for recent acquisitions.

Net income from RBC Global Services was up 44% to \$266 million reflecting fee growth from new business and value-added services added in the investor services business. ROE increased 980 basis points to 49.3%.

Other segment's net income improved to \$(35) million from \$(59) million in 2000. ROE decreased 1,600 basis points to (5.3)%.

Net interest income

Net interest income increased 23% to \$6.5 billion in 2001 from \$5.3 billion in 2000 partially due to the acquisition of Centura Banks, in June 2001 which added more interest-bearing assets and liabilities to the balance sheet.

Non-interest revenue

Non-interest revenue increased 22% to \$8.2 billion in 2001, accounting for 56% of total revenue.

Non-interest expense

Non-interest expense increased 26% to \$9.6 billion, partially reflecting the contribution of expenses from acquisitions and an increase of goodwill amortization expenses associated with these acquisitions.

Taxes

Our income taxes for 2001 were \$1.4 billion, for an effective income tax rate of 34.7%. Income taxes were \$1.4 billion in 2000, reflecting an effective income tax rate was 38.8%.

Provision for credit losses

The provision for credit losses increased 62% to \$1,119 million in 2001 from \$691 million in 2000, largely reflecting increases in business and government provisions for credit losses. The total allowance for loan losses was \$2.3 billion or 1.3% of total loans and acceptances up from 1.1% in 2000.

Quarterly financial information

Selected financial information for the eight most recently completed quarters is shown on page 102.

Consolidated financial statements

Management's responsibility for financial reporting

The accompanying consolidated financial statements of Royal Bank of Canada were prepared by management, which is responsible for the integrity and fairness of the information presented, including the many amounts that must of necessity be based on estimates and judgments. These consolidated financial statements were prepared in accordance with United States generally accepted accounting principles. Financial information appearing throughout this Annual Report is consistent with these consolidated financial statements. Management has also prepared consolidated financial statements for Royal Bank of Canada in accordance with Canadian generally accepted accounting principles, including the accounting requirements of the Superintendent of Financial Institutions Canada, and these consolidated financial statements have also been provided to shareholders.

In discharging its responsibility for the integrity and fairness of the consolidated financial statements and for the accounting systems from which they are derived, management maintains the necessary system of internal controls designed to ensure that transactions are authorized, assets are safeguarded and proper records are maintained. These controls include quality standards in hiring and training of employees, policies and procedures manuals, a corporate code of conduct and accountability for performance within appropriate and well-defined areas of responsibility.

The system of internal controls is further supported by a compliance function, which ensures that the bank and its employees comply with securities legislation and conflict of interest rules, and by an internal audit staff, which conducts periodic audits of all aspects of the bank's operations.

The Board of Directors oversees management's responsibilities for financial reporting through an Audit Committee, which is composed entirely of directors who are neither officers nor employees of the bank.

This Committee reviews the consolidated financial statements of the bank and recommends them to the board for approval. Other key responsibilities of the Audit Committee include reviewing the bank's existing internal control procedures and planned revisions to those procedures, and advising the directors on auditing matters and financial reporting issues. The bank's Compliance Officer and Chief Internal Auditor have full and unrestricted access to the Audit Committee.

At least once a year, the Superintendent of Financial Institutions Canada makes such examination and enquiry into the affairs of the bank as deemed necessary to ensure that the provisions of the *Bank Act*, having reference to the safety of the depositors and shareholders of the bank, are being duly observed and that the bank is in sound financial condition.

Deloitte & Touche LLP and PricewaterhouseCoopers LLP, independent auditors appointed by the shareholders of the bank upon the recommendation of the Audit Committee, have performed an independent audit of the consolidated financial statements and their report follows. The shareholders' auditors have full and unrestricted access to the Audit Committee to discuss their audit and related findings.

Gordon M. Nixon
President & Chief Executive Officer

Peter W. Currie
Vice-Chairman & Chief Financial Officer

Toronto, November 19, 2002

Auditors' report

To the shareholders of Royal Bank of Canada

We have audited the consolidated balance sheet of Royal Bank of Canada as at October 31, 2002 and 2001, and the consolidated statements of income, changes in shareholders' equity and cash flows for each of the years in the three-year period ended October 31, 2002. These consolidated financial statements are the responsibility of the bank's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the bank as at October 31, 2002 and 2001, and the results of its operations and its cash flows for each of the years in the three-year period ended October 31, 2002, in accordance with United States generally accepted accounting principles.

We also reported separately on November 19, 2002, to the shareholders of the bank on our audit, conducted in accordance with Canadian generally accepted auditing standards, where we expressed an opinion without reservation on the October 31, 2002 and 2001, consolidated financial statements, prepared in accordance with Canadian generally accepted accounting principles, including the accounting requirements of the Superintendent of Financial Institutions Canada.

Deloitte & Touche LLP
PricewaterhouseCoopers LLP
Chartered Accountants

Toronto, November 19, 2002

Consolidated balance sheet

As at October 31 (C\$ millions)

| | 2002 | 2001 |
|--|-------------------|-------------------|
| Assets | | |
| Cash resources | | |
| Cash and due from banks | \$ 2,534 | \$ 1,792 |
| Interest-bearing deposits with banks | 18,759 | 15,724 |
| | 21,293 | 17,516 |
| Securities | | |
| Trading account (pledged – \$6,558 and \$4,222) | 69,457 | 58,413 |
| Available for sale | 25,896 | 22,687 |
| | 95,353 | 81,100 |
| Assets purchased under reverse repurchase agreements | 35,831 | 35,870 |
| Loans | | |
| Residential mortgage | 72,842 | 67,444 |
| Personal | 31,956 | 32,511 |
| Credit card | 4,914 | 4,283 |
| Business and government | 61,811 | 66,939 |
| | 171,523 | 171,177 |
| Allowance for loan losses | (2,203) | (2,278) |
| | 169,320 | 168,899 |
| Other | | |
| Customers' liability under acceptances | 8,051 | 9,923 |
| Derivative-related amounts | 31,250 | 28,642 |
| Premises and equipment | 1,639 | 1,598 |
| Goodwill | 5,040 | 4,952 |
| Other intangibles | 665 | 619 |
| Other assets | 13,490 | 13,364 |
| | 60,135 | 59,098 |
| | \$ 381,932 | \$ 362,483 |
| Liabilities and shareholders' equity | | |
| Deposits | | |
| Canada | | |
| Non-interest-bearing | \$ 23,222 | \$ 22,397 |
| Interest-bearing | 119,737 | 118,161 |
| International | | |
| Non-interest-bearing | 2,969 | 2,461 |
| Interest-bearing | 99,112 | 92,668 |
| | 245,040 | 235,687 |
| Other | | |
| Acceptances | 8,051 | 9,923 |
| Obligations related to securities sold short | 17,990 | 16,037 |
| Obligations related to assets sold under repurchase agreements | 21,109 | 20,864 |
| Derivative-related amounts | 32,737 | 29,448 |
| Other liabilities | 29,821 | 23,979 |
| | 109,708 | 100,251 |
| Subordinated debentures | 6,960 | 6,861 |
| Non-controlling interest in subsidiaries | 1,469 | 1,479 |
| Shareholders' equity | | |
| Capital stock | | |
| Preferred | 1,515 | 1,990 |
| Common (shares issued and outstanding – 665,257,068 and 674,020,927) | 7,039 | 6,959 |
| Retained earnings | 10,473 | 9,311 |
| Accumulated other comprehensive income | (272) | (55) |
| | 18,755 | 18,205 |
| | \$ 381,932 | \$ 362,483 |

Gordon M. Nixon
President & Chief Executive Officer

Robert B. Peterson
Director

Consolidated statement of income

For the year ended October 31 (C\$ millions)

| | 2002 | 2001 | 2000 |
|--|-----------------|-----------------|-----------------|
| Interest income | | | |
| Loans | \$ 10,463 | \$ 12,032 | \$ 11,538 |
| Trading account securities | 1,945 | 2,143 | 1,519 |
| Available for sale securities | 1,130 | 1,138 | 1,150 |
| Assets purchased under reverse repurchase agreements | 651 | 1,163 | 1,078 |
| Deposits with banks | 482 | 831 | 824 |
| | 14,671 | 17,307 | 16,109 |
| Interest expense | | | |
| Deposits | 5,709 | 8,712 | 9,057 |
| Other liabilities | 1,405 | 1,688 | 1,429 |
| Subordinated debentures | 406 | 410 | 344 |
| | 7,520 | 10,810 | 10,830 |
| Net interest income | 7,151 | 6,497 | 5,279 |
| Provision for credit losses | 1,065 | 1,119 | 691 |
| | 6,086 | 5,378 | 4,588 |
| Non-interest revenue | | | |
| Capital market fees | 1,866 | 1,523 | 1,538 |
| Trading revenues | 1,766 | 1,820 | 1,540 |
| Investment management and custodial fees | 1,179 | 1,096 | 860 |
| Deposit and payment service charges | 1,041 | 887 | 756 |
| Mutual fund revenues | 723 | 692 | 624 |
| Card service revenues | 285 | 290 | 420 |
| Foreign exchange revenue, other than trading | 277 | 300 | 299 |
| Insurance revenues | 255 | 263 | 151 |
| Mortgage banking revenues | 240 | 206 | - |
| Credit fees | 223 | 237 | 212 |
| Securitization revenues | 172 | 125 | 104 |
| Loss on sale of securities | (95) | (128) | (11) |
| Gain from divestitures | - | 445 | - |
| Other | 647 | 399 | 187 |
| | 8,579 | 8,155 | 6,680 |
| Non-interest expense | | | |
| Human resources | 6,263 | 5,696 | 4,695 |
| Occupancy | 788 | 716 | 570 |
| Equipment | 752 | 713 | 664 |
| Communications | 790 | 679 | 695 |
| Professional fees | 419 | 411 | 267 |
| Amortization of goodwill | - | 252 | 80 |
| Amortization of other intangibles | 72 | 36 | 11 |
| Other | 1,160 | 1,138 | 646 |
| | 10,244 | 9,641 | 7,628 |
| Net income before income taxes | 4,421 | 3,892 | 3,640 |
| Income taxes | 1,415 | 1,350 | 1,412 |
| Net income before non-controlling interest | 3,006 | 2,542 | 2,228 |
| Non-controlling interest in net income of subsidiaries | 108 | 107 | 20 |
| Net income | \$ 2,898 | \$ 2,435 | \$ 2,208 |
| Preferred share dividends | 98 | 135 | 134 |
| Net income available to common shareholders | \$ 2,800 | \$ 2,300 | \$ 2,074 |
| Average number of common shares (in thousands) | 672,571 | 641,516 | 606,389 |
| Earnings per share (in dollars) | \$ 4.16 | \$ 3.58 | \$ 3.42 |
| Average number of diluted common shares (in thousands) | 679,153 | 647,216 | 609,865 |
| Diluted earnings per share (in dollars) | \$ 4.12 | \$ 3.55 | \$ 3.40 |

Consolidated statement of changes in shareholders' equity

| For the year ended October 31 (C\$ millions) | 2002 | 2001 | 2000 |
|---|------------------|------------------|------------------|
| Preferred shares | | | |
| Balance at beginning of year | \$ 1,990 | \$ 2,001 | \$ 1,973 |
| Issued | — | 250 | — |
| Redeemed for cancellation | (464) | (295) | — |
| Issuance costs, net of related income taxes | — | (3) | — |
| Translation adjustment on shares denominated in foreign currency | (11) | 37 | 28 |
| Balance at end of year | 1,515 | 1,990 | 2,001 |
| Common shares | | | |
| Balance at beginning of year | 6,959 | 3,074 | 3,063 |
| Issued | 233 | 4,009 | 109 |
| Issuance costs, net of related income taxes | (1) | (12) | — |
| Purchased for cancellation | (152) | (112) | (98) |
| Balance at end of year | 7,039 | 6,959 | 3,074 |
| Retained earnings | | | |
| Balance at beginning of year | 9,311 | 8,314 | 7,495 |
| Net income | 2,898 | 2,435 | 2,208 |
| Preferred share dividends | (98) | (135) | (134) |
| Common share dividends | (1,022) | (897) | (689) |
| Premium paid on common shares purchased for cancellation | (612) | (397) | (562) |
| Issuance costs, net of related income taxes | (4) | (9) | (4) |
| Balance at end of year | 10,473 | 9,311 | 8,314 |
| Accumulated other comprehensive income (loss), net of related income taxes | | | |
| Unrealized gains and losses on available for sale securities | 202 | 190 | (56) |
| Unrealized foreign currency translation gains and losses, net of hedging activities | (54) | (38) | (36) |
| Gains and losses on derivatives designated as cash flow hedges | (127) | (190) | — |
| Additional pension obligation | (293) | (17) | — |
| Balance at end of year | (272) | (55) | (92) |
| Shareholders' equity at end of year | \$ 18,755 | \$ 18,205 | \$ 13,297 |

Comprehensive income, net of related income taxes

| | | | |
|--|-----------------|-----------------|-----------------|
| Net income | \$ 2,898 | \$ 2,435 | \$ 2,208 |
| Other comprehensive income | | | |
| Change in unrealized gains and losses on available for sale securities | 12 | 246 | 29 |
| Change in unrealized foreign currency translation gains and losses | (59) | 473 | (2) |
| Impact of hedging unrealized foreign currency translation gains and losses | 43 | (475) | 4 |
| Cumulative effect of initial adoption of FAS 133 | — | 60 | — |
| Change in gains and losses on derivatives designated as cash flow hedges | (50) | (250) | — |
| Reclassification to earnings of gains and losses on cash flow hedges | 113 | — | — |
| Additional pension obligation | (276) | (17) | — |
| Total comprehensive income | \$ 2,681 | \$ 2,472 | \$ 2,239 |

Consolidated statement of cash flows

For the year ended October 31 (C\$ millions)

| | 2002 | 2001 | 2000 |
|--|-----------------|-----------------|-----------------|
| Cash flows from operating activities | | | |
| Net income | \$ 2,898 | \$ 2,435 | \$ 2,208 |
| Adjustments to determine net cash provided by (used in) operating activities | | | |
| Provision for credit losses | 1,065 | 1,119 | 691 |
| Depreciation | 388 | 387 | 369 |
| Restructuring | — | 91 | — |
| Amortization of goodwill and other intangibles | 72 | 288 | 91 |
| Deferred income taxes | 45 | 139 | (206) |
| Gain on sale of premises and equipment | (35) | (42) | (4) |
| Gain on divestitures | — | (445) | — |
| Gain on loan securitizations | (54) | (29) | — |
| Loss on sale of available for sale securities | 95 | 128 | 11 |
| Changes in operating assets and liabilities | | | |
| Net change in accrued interest receivable and payable | (166) | (375) | 110 |
| Current income taxes | 419 | (460) | (434) |
| Derivative-related assets | (2,608) | (9,299) | (4,183) |
| Derivative-related liabilities | 3,289 | 10,872 | 3,355 |
| Trading account securities | (11,044) | (8,707) | (13,539) |
| Obligations related to securities sold short | 1,953 | 3,009 | (5,867) |
| Other | 1,610 | (4,920) | (215) |
| Net cash used in operating activities | (2,073) | (5,809) | (17,613) |
| Cash flows from investing activities | | | |
| Change in interest-bearing deposits with banks | (3,035) | (116) | 5,125 |
| Increase in loans, net of loan securitizations | (3,360) | (2,750) | (12,228) |
| Proceeds from loan securitizations | 1,691 | 1,720 | — |
| Proceeds from maturity of held to maturity securities | — | — | 500 |
| Purchases of held to maturity securities | — | — | (114) |
| Proceeds from sale of available for sale securities | 16,758 | 12,542 | 11,033 |
| Proceeds from maturity of available for sale securities | 15,717 | 14,021 | 16,269 |
| Purchases of available for sale securities | (33,450) | (27,975) | (24,385) |
| Net acquisitions of premises and equipment | (390) | (397) | (293) |
| Net proceeds from sale of real estate | — | 57 | — |
| Change in assets purchased under reverse repurchase agreements | 39 | (17,474) | 1,969 |
| Net cash used in acquisition of subsidiaries | (99) | (3,120) | (323) |
| Net proceeds from divestitures | — | 478 | — |
| Net cash used in investing activities | (6,129) | (23,014) | (2,447) |
| Cash flows from financing activities | | | |
| Issue of RBC Trust Capital Securities (RBC TruCS) | — | 750 | 650 |
| Increase in deposits – Canada | 2,402 | 2,434 | 8,818 |
| Increase in deposits – International | 4,997 | 15,690 | 9,405 |
| Issue of subordinated debentures | 635 | 1,025 | 1,200 |
| Maturity of subordinated debentures | (101) | (42) | (20) |
| Redemption of subordinated debentures | (400) | (538) | — |
| Issue of preferred shares | — | 250 | — |
| Redemption of preferred shares for cancellation | (464) | (295) | — |
| Issuance costs | (5) | (24) | (4) |
| Issue of common shares | 168 | 657 | 59 |
| Purchase of common shares for cancellation | (764) | (509) | (660) |
| Payment of dividends | (1,104) | (972) | (791) |
| Change in obligations related to assets sold under repurchase agreements | 245 | 11,629 | (391) |
| Change in short-term borrowings of subsidiaries | 3,335 | (387) | 281 |
| Net cash provided by financing activities | 8,944 | 29,668 | 18,547 |
| Net change in cash and due from banks | 742 | 845 | (1,513) |
| Cash and due from banks at beginning of year | 1,792 | 947 | 2,460 |
| Cash and due from banks at end of year | \$ 2,534 | \$ 1,792 | \$ 947 |
| Supplemental disclosure of cash flow information | | | |
| Amount of interest paid in year | \$ 8,229 | \$ 11,149 | \$ 10,698 |
| Amount of income taxes paid in year | \$ 738 | \$ 1,443 | \$ 2,007 |

NOTE 1 Significant accounting policies

The accompanying consolidated financial statements are stated in Canadian dollars, the currency of the country in which we are incorporated and principally operate. These consolidated financial statements are prepared in accordance with United States generally accepted accounting principles (GAAP) and prevailing practices within the banking industry in that country. We have also prepared consolidated financial statements in accordance with Canadian GAAP and these have been provided to shareholders.

GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements. Actual results could differ from those estimates.

Certain comparative amounts have been reclassified to conform with the current year's presentation.

The significant accounting policies followed in the preparation of these consolidated financial statements are summarized below:

Basis of consolidation

The consolidated financial statements include the assets and liabilities and results of operations of all subsidiaries after elimination of inter-company transactions and balances. We have accounted for the acquisition of subsidiaries using the purchase method. The equity method is used to account for investments in associated corporations or joint ventures in which we have significant influence or exercise joint control, respectively. These investments are reported in Other assets. We have included in Non-interest revenue our share of earnings, and gains and losses realized on dispositions of these investments.

Translation of foreign currencies

Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at rates prevailing on the balance sheet date; income and expenses are translated at average rates of exchange for the year.

Unrealized foreign currency translation gains and losses on investments in foreign branches, subsidiaries and associated corporations where the functional currency is other than the Canadian dollar are recorded in Other comprehensive income. On disposal of such investments, the accumulated net translation gain or loss is included in Non-interest revenue. Other foreign currency translation gains and losses (net of hedging activities) are included in Non-interest revenue.

Securities

Securities are classified, based on management's intentions, as Trading account or Available for sale.

Trading account securities, which are purchased for sale in the near term, are reported at estimated fair value. Obligations to deliver trading account securities sold but not yet purchased are recorded as liabilities and carried at fair value. Realized and unrealized gains and losses on these securities are recorded as Trading revenues in Non-interest revenue. Dividend and interest income accruing on Trading account securities is recorded in Interest income. Interest expense accruing on interest-bearing securities sold short is recorded in Interest expense.

Available for sale securities include securities that may be sold in response to or in anticipation of changes in interest rates and resulting prepayment risk, changes in foreign currency risk, changes in funding sources or terms, or to meet liquidity needs. These securities are carried at estimated fair value. Unrealized gains and losses on these securities, net of income taxes, are reported in Other comprehensive income to the extent not hedged by derivatives. Dividend and interest income is recorded in Interest income. Available for sale securities include tax-exempt securities, which are client financings that have been structured as after-tax investments rather than conventional loans in order to provide the issuers with a borrowing rate advantage.

Gains and losses realized on disposal of Available for sale securities, which are calculated on an average cost basis, and writedowns to reflect other than temporary impairment in value are included in Loss on sale of securities in Non-interest revenue.

Assets purchased under reverse repurchase agreements and sold under repurchase agreements

We purchase securities under agreements to resell (reverse repurchase agreements) and sell securities under agreements to repurchase (repurchase agreements). Reverse repurchase agreements are treated as collateralized lending transactions and are carried on the Consolidated balance sheet at the amounts at which the securities were initially acquired. Repurchase agreements are treated as collateralized borrowing transactions and are carried on the Consolidated balance sheet at the amounts at which the securities were initially sold, plus accrued interest on interest-bearing securities. Interest earned on reverse repurchase agreements and interest incurred on repurchase agreements are included in Interest income and Interest expense, respectively.

Loans

Loans are stated net of an allowance for loan losses and unearned income, which comprises unearned interest and unamortized loan fees.

Loans are classified as nonaccrual when there is no longer reasonable assurance of the timely collection of the full amount of principal or interest. Whenever a payment is 90 days past due, loans other than credit card balances and Canadian government guaranteed loans are classified as nonaccrual unless they are fully secured or collection efforts are reasonably expected to result in repayment of debt. Credit card balances are charged off when a payment is 180 days in arrears. Canadian government guaranteed loans are classified as nonaccrual when the loan is contractually 365 days in arrears. When a loan is identified as nonaccrual, the accrual of interest is discontinued and any previously accrued but unpaid interest on the loan is charged to the Provision for credit losses. Interest received on nonaccrual loans is credited to the Allowance for loan losses on that loan. Nonaccrual loans are returned to performing status when all amounts including interest have been collected, all charges for loan impairment have been reversed and the credit quality has improved such that there is reasonable assurance of timely collection of principal and interest.

When a loan has been identified as nonaccrual, the carrying amount of the loan is reduced to its estimated realizable amount, measured by discounting the expected future cash flows at the effective interest rate inherent in the loan. In subsequent periods, recoveries of amounts previously charged off and any increase in the carrying value of the loan is credited to the Allowance for loan losses on the Consolidated balance sheet. Where a portion of a loan is charged off and the remaining balance is restructured, the new loan is carried on an accrual basis when there is no longer any reasonable doubt regarding the collectibility of principal or interest, and payments are not 90 days past due.

Collateral is obtained if, based on an evaluation of the client's creditworthiness, it is considered necessary for the client's overall borrowing facility.

Assets acquired in respect of problem loans are recorded at the lower of their fair value or the carrying value of the loan at the date of transfer. Any excess of the carrying value of the loan over the fair value of the assets acquired is recognized by a charge to the Allowance for loan losses.

Fees that relate to such activities as originating, restructuring or renegotiating loans are deferred and recognized as Interest income over the expected term of such loans. Where there is reasonable expectation that a loan will result, commitment and standby fees are also recognized as Interest income over the expected term of the resulting loan. Otherwise, such fees are recorded as Other liabilities and amortized to Non-interest revenue over the commitment or standby period.

Allowance for credit losses

The allowance for credit losses is maintained at a level that management considers adequate to absorb identified credit related losses in the portfolio as well as losses that have been incurred, but are not yet identifiable. The allowance relates primarily to loans but also to deposits with banks, derivatives and other credit instruments such as acceptances, guarantees and letters of credit. The allowance is increased by the Provision for credit losses, which is charged to income, and decreased by the amount of charge-offs, net of recoveries.

The allowance is determined based on management's identification and evaluation of problem accounts; estimated probable losses that exist on the remaining portfolio; and on other factors including the composition and quality of the portfolio, and changes in economic conditions.

Allocated specific

Allocated specific allowances are maintained to absorb losses on both specifically identified borrowers and other more homogeneous loans that have been recognized as nonaccrual. The losses relating to identified large business and government debtors are estimated based on the present value of expected payments on an account-by-account basis. The losses relating to other portfolio-type products, excluding credit cards, are based on net charge-off experience over an economic cycle. For credit cards, no specific allowance is maintained as balances are charged off if no payment has been received after 180 days. Personal loans are generally charged off at 150 days past due. Charge-offs for other loans are generally recorded when there is no realistic prospect of full recovery.

Allocated general

The allocated general allowance represents the best estimate of probable losses within the portion of the portfolio that has not yet been specifically identified as nonaccrual. This amount is established through the application of expected loss factors to outstanding and undrawn facilities. The allocated general allowance for large business and government loans and acceptances is based on the application of expected default and loss factors, determined by statistical loss migration analysis, delineated by loan type and rating. For more homogeneous portfolios, such as residential mortgages, small business loans, personal loans and credit cards, the determination of the allocated general allowance is done on a product portfolio basis. The losses are determined by the application of loss ratios determined through the analysis of loss migration and charge-off trends over an economic cycle, adjusted to reflect changes in the product offerings and credit quality of the pool.

Unallocated

The unallocated allowance is based on management's assessment of probable, unidentified losses in the portfolio that have not been captured in the determination of the allocated specific or allocated general allowances. This assessment includes consideration of general economic and business conditions and regulatory requirements affecting key lending operations, recent loan loss experience, and trends in credit quality and concentrations. This allowance also reflects model and estimation risks and does not represent future losses or serve as a substitute for allocated allowances.

Acceptances

Acceptances are short-term negotiable instruments issued by our customers to third parties, which we guarantee. The potential liability under acceptances is reported as a liability in the Consolidated balance sheet. The recourse against the customer in the case of a call on these commitments is reported as a corresponding asset of the same amount in Other assets. Fees earned are reported in Non-interest revenue.

Derivatives

Derivatives are used in sales and trading activities to provide clients with the ability to manage their market risk exposures. Derivatives are also

used to manage our exposures to interest, currency and other market risks. The most frequently used derivative products are foreign exchange forward contracts, interest rate and currency swaps, foreign currency and interest rate futures, forward rate agreements, foreign currency and interest rate options, and credit derivatives. All derivatives, including derivatives embedded in financial instruments or contracts that are not clearly and closely related to the economic characteristics of the host financial instrument or contract, are recorded at fair value on the Consolidated balance sheet.

When used in sales and trading activities, the realized and unrealized gains and losses on derivatives are recognized in Non-interest revenue. Market values are determined using pricing models that incorporate current market and contractual prices of the underlying instruments, time value of money, yield curve and volatility factors. A portion of the market value is deferred within Derivative-related amounts in liabilities and amortized to income over the life of the instruments to cover credit risk and ongoing direct servicing costs. Unrealized gains and losses are generally reported on a gross basis as Derivative-related amounts in assets and liabilities, except where we have both the legal right and intent to settle these amounts simultaneously in which case they are presented on a net basis. Margin requirements and premiums paid are also included in Derivative-related amounts in assets, while premiums received are shown in Derivative-related amounts in liabilities.

When derivatives are used to manage our own exposures, we determine for each derivative whether hedge accounting can be applied. Where hedge accounting can be applied, a hedge relationship is designated as a fair value hedge, a cash flow hedge, or a hedge of foreign currency exposure of net investment in a foreign operation. The hedge is documented at inception detailing the particular risk management objective and the strategy for undertaking the hedge transaction. The documentation identifies the specific asset or liability being hedged, the risk that is being hedged, the type of derivative used and how effectiveness will be measured. The derivative must be highly effective in accomplishing the objective of offsetting either changes in the fair value or cash flows attributable to the risk being hedged both at inception and over the life of the hedge. If it is determined that the derivative is not highly effective as a hedge, hedge accounting is discontinued.

Non-trading derivatives that do not qualify for hedge accounting are carried at fair value on the Consolidated balance sheet, with changes in fair value recorded in Non-interest revenue.

Fair value hedge

Fair value hedge transactions predominantly use interest rate swaps to hedge the changes in the fair value of an asset, liability or firm commitment. The carrying amount of the hedged item is adjusted by gains or losses attributable to the hedged risk and recorded in Non-interest revenue. This unrealized gain or loss is offset by changes in the fair value of the derivative.

Hedge accounting is discontinued prospectively when the derivative no longer qualifies as an effective hedge, the derivative is terminated or sold, or on the sale or early termination of the hedged item. The previously hedged asset or liability is no longer adjusted for changes in fair value. Cumulative fair value adjustments to the carrying amount of the hedged item are amortized into Net interest income over the remaining term of the original hedge relationship.

Cash flow hedge

Cash flow hedge transactions predominantly use interest rate swaps to hedge the variability in cash flows related to a variable rate asset or liability. The effective portion of the changes in the fair value of the derivative is reported in Other comprehensive income. The ineffective portion is reported in Non-interest revenue. The amounts recognized as Other comprehensive income for cash flow hedges are reclassified to Net interest income in the periods in which Net interest income is affected by the variability in the cash flows of the hedged item.

NOTE 1 Significant accounting policies (continued)

Hedge accounting is discontinued prospectively when the derivative no longer qualifies as an effective hedge or the derivative is terminated or sold. The amounts previously recognized in Accumulated other comprehensive income are reclassified to Net interest income in the periods in which Net interest income is affected by the variability in the cash flows of the hedged item. On the sale or early termination of the hedged item, gains and losses are reclassified immediately to Non-interest revenue.

Hedges of net foreign currency investments in subsidiaries

Foreign exchange forward contracts and U.S. dollar liabilities are used to manage exposures from subsidiaries, branches and associated companies having a functional currency other than the Canadian dollar. Foreign exchange gains and losses on these hedging instruments are recorded in Other comprehensive income.

Premises and equipment

Premises and equipment are stated at cost less accumulated depreciation. Depreciation is recorded principally on the straight-line basis over the estimated useful lives of the assets, which are 25 to 50 years for buildings, 3 to 10 years for computer equipment, 7 to 10 years for furniture, fixtures and other equipment, and lease term plus first option period for leasehold improvements. Gains and losses on disposal are recorded in Non-interest revenue.

Business combinations, goodwill and other intangibles

Effective November 1, 2001, we adopted Statement of Financial Accounting Standards, *Goodwill and Other Intangible Assets* (FAS 142) and Statement of Financial Accounting Standards, *Business Combinations* (FAS 141).

The *Business Combinations* standard requires that all business combinations be accounted for using the purchase method. Identifiable intangible assets are recognized separately from Goodwill and included in Other intangibles. Goodwill represents the excess of the price paid for the acquisition of subsidiaries over the fair value of the net assets acquired. Under the *Goodwill and Other Intangible Assets* standard, goodwill and indefinite life intangibles are no longer amortized but are subject to fair value impairment tests on at least an annual basis. Any impairment of goodwill or intangibles will be recognized as Non-interest expense in the period of impairment. Other intangibles with a finite life are amortized over their estimated useful lives and also tested for impairment.

Income taxes

We use the asset and liability method whereby income taxes reflect the expected future tax consequences of temporary differences between the carrying amounts of assets or liabilities for book purposes compared with tax purposes. Accordingly, a deferred income tax asset or liability is determined for each temporary difference based on the tax rates that are expected to be in effect when the underlying items of income and expense are expected to be realized. Income taxes on the consolidated statement of income include the current and deferred portions of the expense. Income taxes applicable to items charged or credited to Shareholders' equity are netted with such items.

Net deferred income taxes accumulated as a result of temporary differences are included in Other assets. A valuation allowance is established to reduce deferred income tax assets to the amount expected to be realized. In addition, the consolidated statement of income contains items that are non-taxable or non-deductible for income tax purposes and, accordingly, cause the income tax provision to be different than what it would be if based on statutory rates.

Pensions and other postretirement benefits

We offer a number of benefit plans which provide pension and other benefits to qualified employees. These plans include statutory pension plans, supplemental pension plans, defined contribution plans and health, dental and life insurance plans.

We fund our statutory pension plans and health, dental and life insurance plans annually based on actuarially determined amounts needed to satisfy employee benefit entitlements under current pension regulations. These pension plans provide benefits based on years of service, contributions and average earnings at retirement.

Actuarial valuations are performed on a regular basis to determine the present value of the accrued pension benefits, based on projections of employees' compensation levels to the time of retirement. Investments held by the pension funds primarily comprise of equity securities, bonds and debentures. Pension fund assets are valued at fair value.

Pension benefit expense consists of the cost of employee pension benefits for the current year's service, interest cost on the liability, expected investment return on the market-related value of plan assets and the amortization of both unrecognized prior service costs and unrecognized net actuarial gains or losses. Amortization is charged over the expected average remaining service life of employee groups covered by the plan.

The cumulative excess of pension fund contributions over the amounts recorded as expenses is reported as a prepaid pension benefit cost in Other assets. The cumulative excess of pension expense over pension fund contributions is reported as accrued pension benefit expense in Other liabilities. In addition, other postretirement benefits are also reported in Other liabilities.

Defined contribution plan costs are recognized in income for services rendered by employees during the period.

Recognition of an additional minimum liability is required if an unfunded accumulated benefit obligation exists and (i) an asset has been recognized as prepaid pension benefit cost, (ii) the liability already recognized as unfunded accrued pension benefit expense is less than the unfunded accumulated benefit obligation, or (iii) no accrued pension benefit expense or prepaid pension benefit cost has been recognized. If an additional liability is required to be recognized and it exceeds unrecognized prior service cost, the excess is reported as Additional pension obligation in Other comprehensive income.

Assets under administration and assets under management

We administer and manage assets owned by clients that are not reflected on the Consolidated balance sheet. Asset management fees are earned for providing investment management services and mutual fund products. Asset administration fees are earned for providing trust, estate administration, custodial services and administration of assets securitized. Fees are recognized and reported in Non-interest revenue as the services are provided.

Loan securitization

We periodically securitize loans by selling loans to independent special purpose entities or trusts that issue securities to investors. These transactions are accounted for as sales when we are deemed to have surrendered control over such assets and have received in exchange consideration other than beneficial interests in these transferred assets. We often retain interests in the securitized loans, such as interest-only strips or servicing rights, and in some cases cash reserve accounts. Gains on these transactions are recognized in Non-interest revenues and are dependent in part on the previous carrying amount of the loans involved in the transfer, which is allocated between the loans sold and the retained interests, based on their relative fair value at the date of transfer. To obtain fair values, quoted market prices are used, if available. When quotes are not available for retained interests, we generally determine fair value based on the present value of expected future cash flows using management's best estimates of key assumptions such as payment rates, excess spread, credit losses and discount rates commensurate with the risks involved.

Generally, the loans are transferred on a fully serviced basis. As a result, we recognize a servicing liability on the date of transfer and amortize this liability to income over the term of the transferred loans.

Retained interests in securitizations that can be contractually pre-paid or otherwise settled in such a way that we would not recover substantially all of our recorded investment, are classified as Available for sale securities.

Insurance operations

Earned premiums, fees and changes in claims and policy benefit liabilities are included in Non-interest revenue. Investments are included in Available for sale securities and claims and policy benefit liabilities are included in Other liabilities. Investment income is included in Interest income and administrative expenses are included in Non-interest expense.

Premiums from long-duration contracts, primarily life insurance, are recognized as income when due, except for universal life and investment-type contracts, the premiums on which are credited to policyholder balances and included in Other liabilities. Premiums from short-duration contracts, primarily property and casualty, and fees for administrative services and investment-type contracts are recognized over the related contract period.

Claims and policy benefit liabilities represent estimates for future insurance policy benefits. Liabilities for life insurance contracts except universal life and investment-type contracts are determined using the net level premium method, which incorporates assumptions for mortality, morbidity, policy lapses and surrenders, investment yields, policy dividends and operating expenses. These assumptions are not revised unless it is determined that existing deferred acquisition costs cannot be recovered. For universal life and investment-type contracts, the liability is equal to the policyholder account values and includes a net level premium reserve for some contracts. Liabilities for property and casualty insurance include unearned premiums, representing the unexpired portion of premiums, and estimated provisions for reported and unreported claims incurred.

Deferred acquisition costs are included in Other assets and amortized to Non-interest revenue and Non-interest expense. Amortization of such costs is in proportion to premium revenue for long-duration contracts, estimated gross profits for universal life and investment-type contracts, and is over the policy term for short-duration contracts.

Value of business acquired represents the present value of estimated net cash flows embedded in existing contracts acquired by us and is included in Other assets. It is amortized in the same manner as deferred acquisition costs for life insurance contracts.

Significant future accounting changes

Stock-based compensation

The Financial Accounting Standards Board issued a proposed statement *Accounting for Stock-Based Compensation – Transition and Disclosure*. This proposal is an amendment to FAS 123 *Accounting for Stock-Based Compensation* and outlines alternative methods of transition for a voluntary change to the fair value method of accounting for stock-based employee compensation. In addition to the prospective application of the fair value recognition provision, retroactive restatement and recognition of stock-based compensation costs as if the fair value provision had been applied to all awards granted, modified or settled after fiscal years beginning after December 15, 1994, is also permitted.

Consolidation of special purpose entities

The Financial Accounting Standards Board issued an Exposure Draft, *Consolidation of Certain Special-Purpose Entities*, on June 28, 2002. The Exposure Draft is an interpretation of Accounting Research Bulletin 51, *Consolidated Financial Statements*, and provides new guidance on determining who is a primary beneficiary of the special purpose entities and will therefore be required to consolidate the special purpose entities. The effect of this Exposure Draft cannot be determined as this time.

NOTE 2 Significant acquisitions and dispositions

2002

Acquisitions

During 2002, we completed the acquisitions of the private banking business of Barclays PLC in the Americas (Barclays) and Eagle Bancshares, Inc. (Eagle Bancshares). Goodwill has been estimated using the best available information as at the date of these financial statements

and may be adjusted for up to one year after the closing date of the acquisition in order to incorporate refinements to the initial fair value estimates of assets and liabilities acquired. The details of these acquisitions are as follows:

| | Barclays | Eagle Bancshares |
|---|---|--|
| Acquisition date | June 28, 2002 | July 22, 2002 |
| Business segment | RBC Investments | RBC Banking |
| Percentage of shares acquired | — | 100% |
| Purchase consideration | Assets were purchased with an initial cash payment of approximately US\$111 million. Additional consideration that is contingent upon the amount of business retained is expected to be paid next year and will be recorded as an intangible asset. | Each Eagle Bancshares common share was purchased for US\$26 cash |
| Fair value of tangible assets acquired | \$ 741 | \$ 1,844 |
| Fair value of liabilities assumed | (640) | (1,764) |
| Fair value of identifiable net tangible assets acquired | 101 | 80 |
| Core deposit intangibles (1) | — | 22 |
| Customer lists and relationships (1) | 68 | — |
| Goodwill | — | 133 |
| Total purchase consideration | \$ 169 | \$ 235 |

(1) Core deposit intangibles and customer lists and relationships are amortized on a straight-line basis over an estimated average useful life of 10 and 15 years, respectively.

NOTE 2 Significant acquisitions and dispositions (continued)**Pending acquisitions***Acquisition of certain U.S. operations of Generali Group*

On April 30, 2002, RBC Insurance announced an agreement to acquire certain assets of Generali Group, the Trieste, Italy-based insurer. These assets consist of the operations of Business Men's Assurance Company of America (BMA) and include an inforce block of approximately 150,000 traditional life insurance policies and annuities as well as the infrastructure for manufacturing variable insurance products. In a related transaction, RBC Dain Rauscher plans to acquire BMA's mutual fund company, Jones & Babson Inc.

The purchase price for these businesses is estimated at approximately US\$220 million. The acquisitions are subject to regulatory approvals, approval by shareholders of advisory clients of Jones & Babson Inc., and other customary closing conditions.

Acquisition of Admiralty Bancorp, Inc.

On August 29, 2002, RBC Centura Banks, Inc. (Centura), a wholly owned subsidiary of Royal Bank of Canada, and Admiralty Bancorp, Inc. (Admiralty) announced that they have signed a definitive merger agreement by which Centura will acquire Admiralty. The cash consideration expected to be paid with respect to the acquisition is approximately US\$150 million. The excess of approximately US\$100 million of the purchase price over the estimated fair value of the net tangible assets acquired will first be allocated to identifiable intangible assets, with the residual allocated to Goodwill. The acquisition is subject to regulatory approvals, approval by shareholders of Admiralty, and other customary closing conditions.

2001**Acquisitions**

During 2001, we completed the acquisitions of Liberty Life Insurance Company and Liberty Insurance Services Corporation (Liberty), Dain Rauscher Corporation (Dain Rauscher), Centura Banks, Inc. (Centura)

and Tucker Anthony Sutro Corporation (Tucker Anthony Sutro). We accounted for all of these acquisitions using the purchase method. The details of these acquisitions are as follows:

| | Liberty | Dain Rauscher | Centura | Tucker Anthony Sutro |
|---|--|---|---|--|
| Acquisition date | November 1, 2000 | January 10, 2001 | June 5, 2001 | October 31, 2001 |
| Business segment | RBC Insurance | RBC Investments & RBC Capital Markets | RBC Banking | RBC Investments & RBC Capital Markets |
| Percentage of shares acquired | 100% | 100% | 100% | 100% |
| Purchase consideration | Assets were purchased with a dividend of US\$70 million paid from Liberty Life Insurance Company plus US\$580 million cash | Each Dain Rauscher common share was purchased for US\$95 cash | Approximately 67 million Royal Bank common shares were issued, valued at \$49.20 each | Each Tucker Anthony Sutro common share was purchased for US\$24 cash |
| Fair value of tangible assets acquired | \$ 2,858 | \$ 3,719 | \$ 18,270 | \$ 831 |
| Fair value of liabilities assumed | (2,095) | (3,425) | (17,214) | (580) |
| Fair value of identifiable net tangible assets acquired | 763 | 294 | 1,056 | 251 |
| Core deposit intangibles (1) | — | — | 395 | — |
| Mortgage servicing rights (1) | — | — | 12 | — |
| Goodwill | 127 | 1,544 | 1,868 | 692 |
| Total purchase consideration | \$ 890 | \$ 1,838 | \$ 3,331 | \$ 943 |

(1) Core deposit intangibles and mortgage servicing rights are amortized on a straight-line basis over an estimated average useful life of 10 and 5 years, respectively.

Dispositions

During 2001, we sold our institutional asset management business operated by RT Capital Management Inc. and realized a pre-tax gain of \$313 million (after-tax \$251 million) recorded in Non-interest revenue.

In addition, we divested certain other businesses and realized a pre-tax gain of \$132 million (after-tax \$111 million) recorded in Non-interest revenue.

NOTE 3 Results by business and geographic segment

| 2002 | RBC Banking | RBC Insurance | RBC Investments | RBC Capital Markets | RBC Global Services | Other | Total | Canada | United States | Other Inter- national |
|--|------------------------|--------------------------|----------------------------|--------------------------------|--------------------------------|--------------|--------------|---------------|--------------------------|--------------------------------------|
| Net interest income on taxable equivalent basis | \$ 5,576 | \$ 223 | \$ 371 | \$ 553 | \$ 136 | \$ 332 | \$ 7,191 | \$ 5,550 | \$ 1,262 | \$ 379 |
| Taxable equivalent adjustment | 19 | — | — | 21 | — | — | 40 | 24 | 16 | — |
| Net interest income | 5,557 | 223 | 371 | 532 | 136 | 332 | 7,151 | 5,526 | 1,246 | 379 |
| Provision for credit losses | 626 | — | (1) | 465 | 10 | (35) | 1,065 | 529 | 440 | 96 |
| | 4,931 | 223 | 372 | 67 | 126 | 367 | 6,086 | 4,997 | 806 | 283 |
| Non-interest revenue | 2,090 | 357 | 3,276 | 2,142 | 672 | 42 | 8,579 | 4,318 | 3,125 | 1,136 |
| Non-interest expense | 4,520 | 399 | 3,144 | 1,627 | 548 | 6 | 10,244 | 5,747 | 3,670 | 827 |
| Net income before income taxes | 2,501 | 181 | 504 | 582 | 250 | 403 | 4,421 | 3,568 | 261 | 592 |
| Income taxes | 947 | (9) | 158 | 143 | 77 | 99 | 1,415 | 1,318 | 49 | 48 |
| Non-controlling interest | 8 | — | — | — | — | 100 | 108 | 100 | 2 | 6 |
| Net income (loss) | \$ 1,546 | \$ 190 | \$ 346 | \$ 439 | \$ 173 | \$ 204 | \$ 2,898 | \$ 2,150 | \$ 210 | \$ 538 |
| Total average assets | \$ 156,500 | \$ 6,900 | \$ 15,100 | \$ 180,700 | \$ 2,400 | \$ 10,100 | \$ 371,700 | \$ 226,800 | \$ 75,800 | \$ 69,100 |

| 2001 | RBC Banking | RBC Insurance | RBC Investments | RBC Capital Markets | RBC Global Services | Other | Total | Canada | United States | Other Inter- national |
|--|------------------------|--------------------------|----------------------------|--------------------------------|--------------------------------|--------------|--------------|---------------|--------------------------|--------------------------------------|
| Net interest income on taxable equivalent basis | \$ 5,349 | \$ 206 | \$ 384 | \$ 429 | \$ 148 | \$ 13 | \$ 6,529 | \$ 5,595 | \$ 485 | \$ 449 |
| Taxable equivalent adjustment | 6 | — | — | 21 | — | 5 | 32 | 30 | 2 | — |
| Net interest income | 5,343 | 206 | 384 | 408 | 148 | 8 | 6,497 | 5,565 | 483 | 449 |
| Provision for credit losses | 732 | — | 2 | 407 | (2) | (20) | 1,119 | 757 | 379 | (17) |
| | 4,611 | 206 | 382 | 1 | 150 | 28 | 5,378 | 4,808 | 104 | 466 |
| Non-interest revenue | 1,873 | 336 | 2,859 | 2,352 | 710 | 25 | 8,155 | 4,862 | 2,404 | 889 |
| Non-interest expense | 4,388 | 375 | 2,510 | 1,804 | 485 | 79 | 9,641 | 6,214 | 2,712 | 715 |
| Net income before income taxes | 2,096 | 167 | 731 | 549 | 375 | (26) | 3,892 | 3,456 | (204) | 640 |
| Income taxes | 912 | (6) | 223 | 200 | 109 | (88) | 1,350 | 1,402 | (68) | 16 |
| Non-controlling interest | 10 | — | — | — | — | 97 | 107 | 97 | 2 | 8 |
| Net income (loss) | \$ 1,174 | \$ 173 | \$ 508 | \$ 349 | \$ 266 | \$ (35) | \$ 2,435 | \$ 1,957 | \$ (138) | \$ 616 |
| Total average assets | \$ 143,000 | \$ 6,300 | \$ 11,300 | \$ 159,500 | \$ 2,400 | \$ 9,100 | \$ 331,600 | \$ 212,700 | \$ 50,900 | \$ 68,000 |

| 2000 | RBC Banking | RBC Insurance | RBC Investments | RBC Capital Markets | RBC Global Services | Other | Total | Canada | United States | Other Inter- national |
|--|------------------------|--------------------------|----------------------------|--------------------------------|--------------------------------|--------------|--------------|---------------|--------------------------|--------------------------------------|
| Net interest income on taxable equivalent basis | \$ 4,705 | \$ 84 | \$ 359 | \$ 43 | \$ 160 | \$ (44) | \$ 5,307 | \$ 5,029 | \$ (17) | \$ 295 |
| Taxable equivalent adjustment | 6 | — | — | 22 | — | — | 28 | 28 | — | — |
| Net interest income | 4,699 | 84 | 359 | 21 | 160 | (44) | 5,279 | 5,001 | (17) | 295 |
| Provision for credit losses | 649 | — | (1) | 91 | (21) | (27) | 691 | 646 | 99 | (54) |
| | 4,050 | 84 | 360 | (70) | 181 | (17) | 4,588 | 4,355 | (116) | 349 |
| Non-interest revenue | 1,569 | 163 | 1,958 | 2,287 | 691 | 12 | 6,680 | 4,962 | 856 | 862 |
| Non-interest expense | 3,776 | 173 | 1,666 | 1,456 | 547 | 10 | 7,628 | 6,245 | 640 | 743 |
| Net income before income taxes | 1,843 | 74 | 652 | 761 | 325 | (15) | 3,640 | 3,072 | 100 | 468 |
| Income taxes | 774 | (29) | 239 | 259 | 140 | 29 | 1,412 | 1,434 | 29 | (51) |
| Non-controlling interest | 5 | — | — | — | — | 15 | 20 | 15 | — | 5 |
| Net income (loss) | \$ 1,064 | \$ 103 | \$ 413 | \$ 502 | \$ 185 | \$ (59) | \$ 2,208 | \$ 1,623 | \$ 71 | \$ 514 |
| Total average assets | \$ 129,700 | \$ 2,200 | \$ 8,000 | \$ 131,900 | \$ 1,600 | \$ 10,700 | \$ 284,100 | \$ 198,800 | \$ 34,800 | \$ 50,500 |

For management reporting purposes, our operations are grouped into the business segments of RBC Banking, RBC Insurance, RBC Investments, RBC Capital Markets and RBC Global Services. The Other segment mainly comprises Corporate Treasury, Corporate Resources, Systems & Technology and Real Estate Operations.

The business segments operate on an arm's-length basis with respect to the purchase and sale of intra-group services. Transfer pricing

of funds sold or purchased, commissions, or charges and credits for services rendered are generally at market rates.

For geographic reporting purposes our operations are grouped into Canada, United States and Other International. Canadian-based activities of international money market units are included in United States and Other International.

NOTE 4 Goodwill and Other intangibles

Effective November 1, 2001, we adopted Statement of Financial Accounting Standards, *Goodwill and Other Intangible Assets* (FAS 142). Under this standard, goodwill impairment is assessed at the reporting unit level on at least an annual basis. Reporting units comprise business operations with similar economic characteristics and strategies and may represent either a business or a business unit within a business segment.

We have completed both the transitional and annual test for goodwill impairment in all reporting units and have determined that goodwill is not impaired.

The projected amortization of Other intangibles for each of the years ending October 31, 2003 to October 31, 2007 is approximately \$76 million.

Goodwill

| | RBC Banking | RBC Insurance | RBC Investments | RBC Capital Markets | RBC Global Services | Total |
|--|-------------|---------------|-----------------|---------------------|---------------------|----------|
| Balance at October 31, 2000 | \$ 200 | \$ 4 | \$ 273 | \$ 93 | \$ 123 | \$ 693 |
| Goodwill acquired during the year | 1,868 | 183 | 1,618 | 618 | 10 | 4,297 |
| Amortization of goodwill during the year | (61) | (15) | (81) | (43) | (14) | (214) |
| Goodwill impairment | — | — | (38) | — | — | (38) |
| Other adjustments (1) | 98 | 24 | 39 | 55 | (2) | 214 |
| Balance at October 31, 2001 | 2,105 | 196 | 1,811 | 723 | 117 | 4,952 |
| Goodwill acquired during the year | 143 | — | — | — | 2 | 145 |
| Other adjustments (1) | (19) | (9) | (19) | (12) | 2 | (57) |
| Balance at October 31, 2002 | \$ 2,229 | \$ 187 | \$ 1,792 | \$ 711 | \$ 121 | \$ 5,040 |

(1) Other adjustments include foreign exchange translations on non-Canadian dollar denominated goodwill and certain other adjustments.

Other intangibles

| | 2002 | | | 2001 | | |
|----------------------------------|-----------------------|--------------------------|---------------------|-----------------------|--------------------------|---------------------|
| | Gross carrying amount | Accumulated amortization | Net carrying amount | Gross carrying amount | Accumulated amortization | Net carrying amount |
| Core deposit intangibles | \$ 423 | \$ (50) | \$ 373 | \$ 412 | \$ (17) | \$ 395 |
| Customer lists and relationships | 318 | (52) | 266 | 233 | (30) | 203 |
| Mortgage servicing rights | 41 | (18) | 23 | 17 | (1) | 16 |
| Other intangibles | 5 | (2) | 3 | 7 | (2) | 5 |
| Total | \$ 787 | \$ (122) | \$ 665 | \$ 669 | \$ (50) | \$ 619 |

The following table discloses a reconciliation of reported net income, earnings per share and diluted earnings per share to the amounts adjusted for the exclusion of Amortization of goodwill, net of related income taxes.

| | 2002 | 2001 | 2000 |
|---|----------|----------|----------|
| Net income: | | | |
| Reported net income | \$ 2,898 | \$ 2,435 | \$ 2,208 |
| Amortization of goodwill, net of related income taxes | — | 250 | 77 |
| Adjusted net income | \$ 2,898 | \$ 2,685 | \$ 2,285 |
| Earnings per share: | | | |
| Reported earnings per share | \$ 4.16 | \$ 3.58 | \$ 3.42 |
| Amortization of goodwill, net of related income taxes | — | .39 | .13 |
| Adjusted earnings per share | \$ 4.16 | \$ 3.97 | \$ 3.55 |
| Diluted earnings per share: | | | |
| Reported diluted earnings per share | \$ 4.12 | \$ 3.55 | \$ 3.40 |
| Amortization of goodwill, net of related income taxes | — | .39 | .13 |
| Adjusted diluted earnings per share | \$ 4.12 | \$ 3.94 | \$ 3.53 |

NOTE 5 Securities

| | Term to maturity (1) | | | | | 2002 Total | 2001 Total |
|---|----------------------|-----------------|-----------------------------|------------------|---------------------------------|-----------------|-----------------|
| | Under 1 year | 1 to 5 years | Over 5 years to 10 years | Over 10 years | With no specific maturity | | |
| Trading account (2) | | | | | | | |
| Canadian government debt | \$ 5,226 | \$ 4,344 | \$ 1,533 | \$ 1,572 | \$ – | \$12,675 | \$13,024 |
| U.S. Treasury and other U.S. agencies | 278 | 720 | 593 | 24 | – | 1,615 | 1,148 |
| Other OECD government debt | 618 | 1,223 | 1,254 | 738 | – | 3,833 | 2,413 |
| Mortgage-backed securities | 74 | 125 | 86 | 327 | – | 612 | 689 |
| Asset-backed securities | 65 | 248 | 2,704 | 3,522 | – | 6,539 | 4,428 |
| Other debt | 9,253 | 4,265 | 2,001 | 2,906 | 579 | 19,004 | 20,785 |
| Equities | – | – | – | – | 25,179 | 25,179 | 15,926 |
| | 15,514 | 10,925 | 8,171 | 9,089 | 25,758 | 69,457 | 58,413 |
| Available for sale (2) | | | | | | | |
| Canadian government debt | | | | | | | |
| Amortized cost | 1,943 | 2,826 | 503 | 247 | – | 5,519 | 4,623 |
| Estimated fair value | 1,945 | 2,883 | 510 | 275 | – | 5,613 | 4,708 |
| Yield (3) | 4.0% | 4.5% | 5.3% | 6.6% | – | 4.5% | 4.9% |
| U.S. Treasury and other U.S. agencies | | | | | | | |
| Amortized cost | 544 | 1,204 | 319 | 1 | – | 2,068 | 2,030 |
| Estimated fair value | 552 | 1,280 | 355 | 1 | – | 2,188 | 2,118 |
| Yield (3) | 4.0% | 5.0% | 3.9% | 6.0% | – | 4.6% | 4.8% |
| Other OECD government debt | | | | | | | |
| Amortized cost | 2,308 | 291 | 6 | – | – | 2,605 | 1,561 |
| Estimated fair value | 2,324 | 303 | 6 | – | – | 2,633 | 1,573 |
| Yield (3) | .3% | 3.7% | 4.7% | – | – | .7% | 1.2% |
| Mortgage-backed securities | | | | | | | |
| Amortized cost | 1,126 | 2,730 | 294 | 435 | – | 4,585 | 4,531 |
| Estimated fair value | 1,136 | 2,782 | 312 | 457 | – | 4,687 | 4,676 |
| Yield (3) | 5.0% | 5.0% | 7.2% | 6.5% | – | 5.3% | 5.6% |
| Asset-backed securities | | | | | | | |
| Amortized cost | – | 98 | 154 | 75 | – | 327 | 414 |
| Estimated fair value | – | 98 | 163 | 83 | – | 344 | 434 |
| Yield (3) | – | 8.3% | 6.8% | 6.6% | – | 7.2% | 8.2% |
| Other debt | | | | | | | |
| Amortized cost | 2,304 | 1,815 | 593 | 4,198 | 159 | 9,069 | 7,716 |
| Estimated fair value | 2,300 | 1,853 | 612 | 4,267 | 159 | 9,191 | 7,760 |
| Yield (3) | 2.3% | 4.1% | 6.1% | 5.4% | 5.1% | 4.4% | 5.6% |
| Equities | | | | | | | |
| Cost | – | – | – | – | 1,272 | 1,272 | 1,382 |
| Estimated fair value | – | – | – | – | 1,240 | 1,240 | 1,418 |
| Amortized cost | 8,225 | 8,964 | 1,869 | 4,956 | 1,431 | 25,445 | 22,257 |
| Estimated fair value | 8,257 | 9,199 | 1,958 | 5,083 | 1,399 | 25,896 | 22,687 |
| Total carrying value of securities (2) | \$23,771 | \$20,124 | \$10,129 | \$14,172 | \$27,157 | \$95,353 | \$81,100 |

(1) Actual maturities may differ from contractual maturities shown above, since borrowers may have the right to prepay obligations with or without prepayment penalties.

(2) Trading account and Available for sale securities are carried at estimated fair value.

(3) The weighted average yield is based on the carrying value at the end of the year for the respective securities.

Unrealized gains and losses on Available for sale securities

| | 2002 | | | | 2001 | | | |
|---------------------------------------|-------------------|------------------------------|-------------------------------|----------------------------|-------------------|------------------------------|-------------------------------|----------------------------|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | Estimated fair value | Amortized cost | Gross unrealized gains | Gross unrealized losses | Estimated fair value |
| Canadian government debt | \$ 5,519 | \$ 97 | \$ (3) | \$ 5,613 | \$ 4,623 | \$ 85 | \$ – | \$ 4,708 |
| U.S. Treasury and other U.S. agencies | 2,068 | 120 | – | 2,188 | 2,030 | 88 | – | 2,118 |
| Other OECD government debt | 2,605 | 28 | – | 2,633 | 1,561 | 15 | (3) | 1,573 |
| Mortgage-backed securities | 4,585 | 102 | – | 4,687 | 4,531 | 145 | – | 4,676 |
| Asset-backed securities | 327 | 28 | (11) | 344 | 414 | 25 | (5) | 434 |
| Other debt | 9,069 | 201 | (79) | 9,191 | 7,716 | 169 | (125) | 7,760 |
| Equities | 1,272 | 28 | (60) | 1,240 | 1,382 | 104 | (68) | 1,418 |
| | \$25,445 | \$ 604 | \$ (153) | \$25,896 | \$22,257 | \$ 631 | \$ (201) | \$22,687 |

Realized gains and losses on sale of Available for sale securities

| | 2002 | 2001 | 2000 |
|----------------------------|---------|----------|---------|
| Realized gains | \$ 102 | \$ 106 | \$ 106 |
| Realized losses | (197) | (234) | (117) |
| Loss on sale of securities | \$ (95) | \$ (128) | \$ (11) |

NOTE 6 Loans

| | 2002 | 2001 |
|---|------------|------------|
| Canada ⁽¹⁾ | | |
| Residential mortgage | \$ 67,700 | \$ 64,066 |
| Personal | 25,918 | 27,202 |
| Credit card | 4,740 | 4,110 |
| Business and government | 29,832 | 32,739 |
| | 128,190 | 128,117 |
| United States ⁽¹⁾ | | |
| Residential mortgage | 4,353 | 2,666 |
| Personal | 5,269 | 4,621 |
| Credit card | 125 | 128 |
| Business and government | 21,418 | 22,145 |
| | 31,165 | 29,560 |
| Other International ⁽¹⁾ | | |
| Residential mortgage | 789 | 712 |
| Personal | 769 | 688 |
| Credit card | 49 | 45 |
| Business and government | 10,561 | 12,055 |
| | 12,168 | 13,500 |
| Total loans ⁽²⁾ | 171,523 | 171,177 |
| Allowance for loan losses | (2,203) | (2,278) |
| Total loans net of allowance for loan losses | \$ 169,320 | \$ 168,899 |

(1) Loans in Canada, United States and Other International include all loans booked in those locations, regardless of currency or residence of borrower.

(2) Loans are net of unearned income of \$131 million (2001 – \$130 million).

Loan maturities and rate sensitivity 2002

| | Maturity term | | | | Rate sensitivity | | | |
|---|---------------|--------------|--------------|------------|------------------|------------|--------------------|------------|
| | Under 1 year | 1 to 5 years | Over 5 years | Total | Floating | Fixed term | Non-rate-sensitive | Total |
| Residential mortgage | \$ 27,491 | \$ 44,057 | \$ 1,294 | \$ 72,842 | \$ 8,128 | \$ 64,583 | \$ 131 | \$ 72,842 |
| Personal | 30,363 | 1,486 | 107 | 31,956 | 21,934 | 9,716 | 306 | 31,956 |
| Credit card | 4,914 | — | — | 4,914 | — | 3,326 | 1,588 | 4,914 |
| Business and government | 45,046 | 13,242 | 3,523 | 61,811 | 14,054 | 45,906 | 1,851 | 61,811 |
| Total loans | \$ 107,814 | \$ 58,785 | \$ 4,924 | 171,523 | \$ 44,116 | \$ 123,531 | \$ 3,876 | 171,523 |
| Allowance for loan losses | | | | (2,203) | | | | (2,203) |
| Total loans net of allowance for loan losses | | | | \$ 169,320 | | | | \$ 169,320 |

Nonaccrual loans

| | 2002 | 2001 |
|---|----------|----------|
| Residential mortgage | \$ 131 | \$ 179 |
| Personal | 306 | 325 |
| Business and government | 346 | 372 |
| | 783 | 876 |
| Individually impaired business and government | 1,505 | 1,589 |
| | \$ 2,288 | \$ 2,465 |
| Allowance for impaired loans | \$ 555 | \$ 614 |
| Average balance of impaired loans ⁽¹⁾ | \$ 1,607 | \$ 1,190 |

(1) For the year ended October 31, 2000, the average balance of impaired loans was \$941 million.

Allowance for loan losses

| | 2002 | 2001 | 2000 |
|---|----------|----------|----------|
| Allowance for credit losses at beginning of year | \$ 2,392 | \$ 1,975 | \$ 1,900 |
| Charge-offs | (1,457) | (1,125) | (839) |
| Recoveries | 198 | 185 | 162 |
| Net charge-offs | (1,259) | (940) | (677) |
| Provision for credit losses | 1,065 | 1,119 | 691 |
| Acquisition of Centura Banks, Inc. | — | 157 | — |
| Acquisition of Eagle Bancshares, Inc. | 18 | — | — |
| Other | 98 | 81 | 61 |
| Allowance for credit losses at end of year | 2,314 | 2,392 | 1,975 |
| Allowance for off-balance sheet and other items (1) | (109) | (109) | (98) |
| Allowance for securities | (2) | (5) | (6) |
| Allowance for loan losses at end of year | \$ 2,203 | \$ 2,278 | \$ 1,871 |

(1) The allowance for off-balance sheet and other items is included in Other liabilities.

NOTE 7 Securitizations

During the year, we securitized \$3,734 million (2001 – \$800 million) of government guaranteed residential mortgage loans through the creation of mortgage-backed securities, and sold \$1,708 million (2001 – \$723 million) of those securities. We received net cash proceeds of \$1,691 million (2001 – \$720 million) and retained the rights to future excess interest of \$71 million (2001 – \$25 million) on the residential mortgages. A pre-tax gain on sale, net of transaction costs, of \$54 million (2001 – \$22 million) was recognized in Securitization revenues. Mortgage-backed securities, created and unsold, remain on the Consolidated balance sheet and are classified as Available for sale.

We did not sell any undivided interests in credit card loans during the year (2001 – \$1,000 million).

The key assumptions used to value the retained interests in residential mortgage loans at the date of securitization for transactions completed during the year were an annualized payment rate of 12.00%, excess spread of 1.20%, and discount rate of 4.75%.

Static pool credit losses include actual incurred and projected credit losses divided by the original balance of the loans securitized. The expected static pool credit loss ratio for securitized credit card loans at October 31, 2002 was .41%.

The following table summarizes the loan principal, nonaccrual and net charge-offs for total loans reported on our balance sheet and securitized loans that we manage as at October 31, 2002 and 2001:

Loans reported and securitized

| | 2002 | | | 2001 | | |
|--|----------------|----------------|-----------------|----------------|----------------|-----------------|
| | Loan principal | Nonaccrual (1) | Net charge-offs | Loan principal | Nonaccrual (1) | Net charge-offs |
| Residential mortgage | \$ 78,323 | \$ 228 | \$ 12 | \$ 71,884 | \$ 283 | \$ 24 |
| Personal | 31,956 | 371 | 328 | 32,511 | 387 | 334 |
| Credit card | 6,589 | 41 | 172 | 6,383 | 49 | 152 |
| Business and government | 61,811 | 1,865 | 779 | 66,939 | 1,991 | 455 |
| Total loans managed (2) | 178,679 | 2,505 | 1,291 | 177,717 | 2,710 | 965 |
| Less: Loans securitized (3) | 7,156 | — | 32 | 6,540 | — | 25 |
| Total loans reported on the Consolidated balance sheet | \$ 171,523 | \$ 2,505 | \$ 1,259 | \$ 171,177 | \$ 2,710 | \$ 940 |

(1) Includes past due loans greater than 90 days not classified as nonaccrual.

(2) Represents net loans outstanding and loans that have been securitized, which we continue to service, and excludes any assets we have temporarily acquired with the intent at acquisition to sell them to special purpose entities.

(3) Loan principal includes credit card loans of \$1,675 million (2001 – \$2,100 million), mortgage-backed securities created and sold of \$2,416 million (2001 – \$1,361 million) and mortgage-backed securities created and unsold of \$3,065 million (2001 – \$3,079 million).

NOTE 7 **Securitizations** (continued)

At October 31, 2002, key economic assumptions and the sensitivity of the current fair value of these retained interests to immediate 10% and 20% adverse changes in key assumptions are shown in the first table below.

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in fair value based on a variation in assumptions generally cannot be extrapolated because the relationship

of the change in assumption to the change in fair value may not be linear. Also, the effect of a variation in a particular assumption on the fair value of the retained interests is calculated without changing any other assumption; generally, changes in one factor may result in changes in another, which may magnify or counteract the sensitivities.

The second table below summarizes certain cash flows received from securitizations in 2002 and 2001.

Sensitivity of key assumptions to adverse changes ⁽¹⁾

| | Impact on fair value | |
|--|----------------------|----------------------------|
| | Credit card loans | Residential mortgage loans |
| Fair value of retained interests | \$ 15.1 | \$ 94.6 |
| Weighted average remaining service life (in years) | .2 | 3.9 |
| Payment rate | 39.07% | 13.62% |
| Impact on fair value of 10% adverse change | \$ (1.0) | \$ (2.7) |
| Impact on fair value of 20% adverse change | (1.9) | (5.3) |
| Excess spread, net of credit losses | 5.92% | 1.19% |
| Impact on fair value of 10% adverse change | \$ (1.5) | \$ (9.5) |
| Impact on fair value of 20% adverse change | (3.1) | (18.9) |
| Expected credit losses | 1.68% | — |
| Impact on fair value of 10% adverse change | \$ (.5) | — |
| Impact on fair value of 20% adverse change | (.9) | — |
| Discount rate | 12.50% | 4.55% |
| Impact on fair value of 10% adverse change | \$ (.1) | \$ (.3) |
| Impact on fair value of 20% adverse change | (.1) | (.6) |

(1) All rates are annualized except for credit card loans payment rate, which is monthly.

Cash flows from securitizations

| | 2002 | | 2001 | |
|---|-------------------|----------------------------|-------------------|----------------------------|
| | Credit card loans | Residential mortgage loans | Credit card loans | Residential mortgage loans |
| Proceeds from new securitizations | \$ — | \$ 1,691 | \$ 1,000 | \$ 720 |
| Proceeds reinvested in revolving securitizations | 8,512 | 303 | 6,972 | 13 |
| Cash flows from retained interests in securitizations | 64 | 15 | 60 | 10 |

NOTE 8 Premises and equipment

| | 2002 | | | 2001 |
|---|-----------------|--------------------------|-----------------|-----------------|
| | Cost | Accumulated depreciation | Net book value | Net book value |
| Land | \$ 172 | \$ — | \$ 172 | \$ 123 |
| Buildings | 606 | 287 | 319 | 335 |
| Computer equipment | 1,605 | 1,163 | 442 | 437 |
| Furniture, fixtures and other equipment | 976 | 650 | 326 | 313 |
| Leasehold improvements | 901 | 521 | 380 | 390 |
| | \$ 4,260 | \$ 2,621 | \$ 1,639 | \$ 1,598 |

The depreciation and amortization expense for premises and equipment amounted to \$388 million and \$387 million in 2002 and 2001, respectively.

NOTE 9 Other assets

| | 2002 | 2001 |
|--|------------------|------------------|
| Receivable from brokers, dealers and clients | \$ 3,229 | \$ 3,505 |
| Insurance-related assets (1) | 2,987 | 2,043 |
| Accrued interest receivable | 1,287 | 1,733 |
| Net deferred income tax asset | 1,003 | 1,047 |
| Investment in associated corporations | 224 | 152 |
| Prepaid pension benefit cost (2) | 109 | 366 |
| Other | 4,651 | 4,518 |
| | \$ 13,490 | \$ 13,364 |

- (1) Insurance-related assets include, among other items, policy loan balances, premiums outstanding, amounts due from other insurers in respect of reinsurance contracts and pooling arrangements, deferred acquisition costs and value of business acquired.
- (2) Prepaid pension benefit cost represents the cumulative excess of pension fund contributions over the amounts recorded as pension benefit expense.

NOTE 10 Deposits

| | 2002 | | | | 2001 |
|-----------------------------|------------------|------------------|-------------------|-------------------|-------------------|
| | Demand (1) | Notice (2) | Term (3) | Total | Total |
| Personal | \$ 10,735 | \$ 30,065 | \$ 61,092 | \$ 101,892 | \$ 101,381 |
| Business and government | 39,004 | 8,864 | 71,898 | 119,766 | 107,485 |
| Bank | 3,084 | 85 | 20,213 | 23,382 | 26,821 |
| | \$ 52,823 | \$ 39,014 | \$ 153,203 | \$ 245,040 | \$ 235,687 |
| Non-interest-bearing | | | | | |
| Canada | | | | \$ 23,222 | \$ 22,397 |
| United States | | | | 2,078 | 1,918 |
| Other International | | | | 891 | 543 |
| Interest-bearing | | | | | |
| Canada | | | | 119,737 | 118,161 |
| United States | | | | 35,495 | 25,169 |
| Other International | | | | 63,617 | 67,499 |
| | | | | \$ 245,040 | \$ 235,687 |

- (1) Deposits payable on demand include all deposits for which we do not have the right to notice of withdrawal. These deposits are for the most part, chequing accounts.
- (2) Deposits payable after notice include all deposits for which we can legally require notice of withdrawal. These deposits are for the most part, savings accounts.
- (3) Term deposits include deposits payable on a fixed date. These deposits include term deposits, guaranteed investment certificates and similar instruments. At October 31, 2002, the balance of term deposits also includes senior deposit notes we have issued to provide long-term funding of \$11.3 billion (2001 – \$10.7 billion) and other notes and similar instruments in bearer form we have issued of \$21.7 billion (2001 – \$18.5 billion).

NOTE 11 Other liabilities

| | 2002 | 2001 |
|--|------------------|------------------|
| Short-term borrowings of subsidiaries | \$ 10,173 | \$ 6,838 |
| Insurance claims and policy benefit liabilities | 5,302 | 4,256 |
| Payable to brokers, dealers and clients | 3,630 | 3,202 |
| Accrued interest payable | 1,263 | 1,887 |
| Accrued pension and other postretirement benefit expense (1) | 919 | 714 |
| Dividends payable | 289 | 273 |
| Other | 8,245 | 6,809 |
| | \$ 29,821 | \$ 23,979 |

(1) Accrued pension and other postretirement benefit expense represents the cumulative excess of pension and other postretirement benefit expense over pension fund contributions.

NOTE 12 Subordinated debentures

The debentures are unsecured obligations and are subordinated in right of payment to the claims of depositors and certain other creditors. All redemptions, cancellations and exchanges of subordinated debentures are subject to the consent and approval of the Superintendent of Financial Institutions Canada.

| Maturity | Earliest par value redemption date | Interest rate | Denominated in foreign currency | 2002 | 2001 |
|----------------------------|------------------------------------|---------------|---------------------------------|-----------------|-----------------|
| January 11, 2002 | | 11.00% | | \$ – | \$ 41 |
| March 1, 2002 | | 10.50% | | – | 60 |
| September 3, 2007 | | 5.40% (1) | | – | 400 |
| September 3, 2008 | September 3, 2003 (2) | 5.45% (3) | | 100 | 100 |
| March 15, 2009 | | 6.50% | US\$125 | 195 | 199 |
| April 12, 2009 | April 12, 2004 (2) | 5.40% (3) | | 350 | 350 |
| June 11, 2009 | June 11, 2004 (2) | 5.10% (3) | | 350 | 350 |
| July 7, 2009 | July 7, 2004 (2) | 6.05% (3) | | 175 | 175 |
| October 12, 2009 | October 12, 2004 (2) | 6.00% (3) | | 150 | 150 |
| August 15, 2010 | August 15, 2005 (2) | 6.40% (3) | | 700 | 700 |
| February 13, 2011 | February 13, 2006 (4) | 5.50% (3) | | 125 | 125 |
| April 26, 2011 | April 26, 2006 (5) | 8.20% (3) | | 100 | 100 |
| September 12, 2011 | September 12, 2006 (2) | 6.50% (3) | | 350 | 350 |
| October 24, 2011 | October 24, 2006 (6) | 6.75% (7) | US\$300 | 467 | 476 |
| November 8, 2011 | November 8, 2006 (8) | (9) | US\$400 | 625 | – |
| June 4, 2012 | June 4, 2007 (2) | 6.75% (3) | | 500 | 500 |
| January 22, 2013 | January 22, 2008 (10) | 6.10% (3) | | 500 | 500 |
| November 14, 2014 | | 10.00% | | 200 | 200 |
| January 25, 2015 | January 25, 2010 (11) | 7.10% (3) | | 500 | 500 |
| April 12, 2016 | April 12, 2011 (12) | 6.30% (3) | | 400 | 400 |
| June 8, 2023 | | 9.30% | | 110 | 110 |
| October 1, 2083 | (13) | (14) | | 250 | 250 |
| June 6, 2085 | (13) | (15) | US\$300 | 467 | 477 |
| | | | | 6,614 | 6,513 |
| Fair value adjustment (16) | | | | 346 | 348 |
| | | | | \$ 6,960 | \$ 6,861 |

(1) Redeemed on September 3, 2002 at par value.

(2) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on Government of Canada bonds plus 5 basis points and (ii) par value, and thereafter at any time at par value.

(3) Interest at stated interest rate until earliest par value redemption date, and thereafter at a rate of 1.00% above the 90-day Bankers' Acceptance rate.

(4) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on Government of Canada bonds plus 8 basis points and (ii) par value, and thereafter at any time at par value.

(5) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on Government of Canada bonds plus 10 basis points and (ii) par value, and thereafter at any time at par value.

(6) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on U.S. Treasury notes plus 10 basis points and (ii) par value, and thereafter at any time at par value.

(7) Interest at a rate of 6.75% until earliest par value redemption date, and thereafter at a rate of 1.00% above the U.S. dollar 6-month LIBOR.

(8) Redeemable on the earliest par value redemption date at par value.

(9) Interest at a rate of .50% above the U.S. dollar 3-month LIBOR until earliest par value redemption date, and thereafter at a rate of 1.50% above the U.S. dollar 3-month LIBOR.

(10) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on Government of Canada bonds plus 18 basis points and (ii) par value, and thereafter at any time at par value.

(11) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on Government of Canada bonds plus 12.5 basis points and (ii) par value, and thereafter at any time at par value.

(12) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on Government of Canada bonds plus 22 basis points and (ii) par value, and thereafter at any time at par value.

(13) Redeemable on any interest payment date at par value.

(14) Interest at a rate of .40% above the 30-day Bankers' Acceptance rate.

(15) Interest at a rate of .25% above the U.S. dollar 3-month LIMEAN. In the event of a reduction of the annual dividend we declare on our common shares, the interest payable on the debentures is reduced pro rata to the dividend reduction and the interest reduction is payable with the proceeds from the sale of newly issued common shares.

(16) The fair value adjustment reflects the adjustment to the carrying value of hedged subordinated debentures as a result of FAS 133. The subordinated debentures specifically hedged have maturity dates ranging from October 24, 2011 to April 12, 2016.

NOTE 12 Subordinated debentures (continued)**Maturity schedule**

The aggregate maturities of subordinated debentures, based on the maturity dates under the terms of issue, are as follows:

| | |
|--------------|-----------------|
| 2003 – 2007 | \$ – |
| 2008 to 2012 | 4,310 |
| Thereafter | 2,650 |
| | \$ 6,960 |

NOTE 13 Capital stock**Authorized capital stock**

Preferred – An unlimited number of First Preferred Shares and Second Preferred Shares without nominal or par value, issuable in series; the aggregate consideration for which all the First Preferred Shares and all the Second Preferred Shares that may be issued may not exceed \$10 billion and \$5 billion, respectively.

Common – An unlimited number of shares without nominal or par value may be issued.

Issued and outstanding capital stock

| | 2002 | | | 2001 | | | 2000 | | |
|--|-------------------------|-----------------|------------------------------|-------------------------|-----------------|------------------------------|-------------------------|-----------------|------------------------------|
| | Number of shares (000s) | Amount | Dividends declared per share | Number of shares (000s) | Amount | Dividends declared per share | Number of shares (000s) | Amount | Dividends declared per share |
| First Preferred | | | | | | | | | |
| Non-cumulative Series E (1) | – | \$ – | \$ 3.06 | 1,500 | \$ 149 | \$ 5.16 | 1,500 | \$ 149 | \$ 5.38 |
| Non-cumulative Series H (1) | – | – | – | – | – | 1.69 | 12,000 | 295 | 2.25 |
| US\$ Non-cumulative Series I (1) | – | – | US .02 | 8,000 | 315 | US 1.91 | 8,000 | 301 | US 1.91 |
| Non-cumulative Series J | 12,000 | 294 | 1.78 | 12,000 | 294 | 1.78 | 12,000 | 294 | 1.78 |
| US\$ Non-cumulative Series K | 10,000 | 384 | US 1.58 | 10,000 | 392 | US 1.58 | 10,000 | 376 | US 1.58 |
| Non-cumulative Series N | 12,000 | 293 | 1.18 | 12,000 | 293 | 1.18 | 12,000 | 293 | 1.18 |
| Non-cumulative Series O | 6,000 | 145 | 1.38 | 6,000 | 145 | 1.38 | 6,000 | 145 | 1.38 |
| US\$ Non-cumulative Series P | 4,000 | 152 | US 1.44 | 4,000 | 155 | US 1.44 | 4,000 | 148 | US 1.44 |
| Non-cumulative Series S | 10,000 | 247 | 1.53 | 10,000 | 247 | .65 | – | – | – |
| | | \$ 1,515 | | | \$ 1,990 | | | \$ 2,001 | |
| Common | | | | | | | | | |
| Balance at beginning of year | 674,021 | \$ 6,959 | | 602,398 | \$ 3,074 | | 617,768 | \$ 3,063 | |
| Issued | – | – | | 12,305 | 576 | | – | – | |
| Issued under the stock option plan (2) | 5,211 | 175 | | 2,819 | 81 | | 2,700 | 59 | |
| Issued on the acquisition of Centura Banks, Inc. | – | – | | 67,413 | 3,317 | | – | – | |
| Options granted on acquisition of Dain Rauscher Corporation | – | 14 | | – | 33 | | – | – | |
| Issued on the acquisition of Richardson Greenshields Limited (3) | 318 | 15 | | 13 | 2 | | 1,667 | 50 | |
| Renounced stock appreciation rights, net of related income taxes | – | 29 | | – | – | | – | – | |
| Issuance costs, net of related income taxes | – | (1) | | – | (12) | | – | – | |
| Purchased for cancellation (4) | (14,293) | (152) | | (10,927) | (112) | | (19,737) | (98) | |
| Balance at end of year | 665,257 | \$ 7,039 | \$ 1.51 | 674,021 | \$ 6,959 | \$ 1.38 | 602,398 | \$ 3,074 | \$ 1.14 |

- On November 26, 2001 and October 11, 2002, we redeemed First Preferred Shares Series I and E respectively. On August 24, 2001 we redeemed First Preferred Shares Series H.
- Includes the exercise of stock options from tandem stock appreciation rights awards, resulting in a reversal of the accrued liability, net of related income taxes, of \$8 million.
- During the year we exchanged nil (2001 – 36,527; 2000 – 4,701) Class B shares and 1,846,897 (2001 – 77,956; 2000 – 8,008,712) Class C shares issued by our wholly owned subsidiary, Royal Bank DS Holding Inc., on the acquisition of Richardson Greenshields Limited for 318,154 (2001 – 13,621; 2000 – 1,667,334) common shares.
- Commencing in June 2001, pursuant to a one-year normal course issuer bid, we repurchased through the facilities of the Toronto and Montreal Stock Exchanges 15,401,100 common shares at an average price of \$49.32 per share. Under this bid, 10,927,200 common shares were repurchased during fiscal 2001 at a cost of \$509 million and 4,473,900 common shares were repurchased during fiscal 2002 at a cost of \$251 million. On June 24, 2002, we renewed our one-year normal course issuer bid to purchase for cancellation, up to 20 million of our common shares, representing approximately 3% of our outstanding common shares. Under this renewed bid, 9,818,900 common shares were purchased, at an average cost of \$52.27 per share, for \$513 million. During fiscal 2002, a total of 14,292,800 common shares were repurchased for \$764 million at an average cost of \$53.45 per share.

NOTE 13 Capital stock (continued)

Terms of preferred shares

| | Dividend per share (1) | Redemption date (2) | Redemption price (3) | Conversion dates | |
|------------------------------|---------------------------|------------------------|-------------------------|---------------------------------------|------------------------------------|
| | | | | At the option of the bank (2), (4) | At the option of the holder (5) |
| First Preferred | | | | | |
| Non-cumulative Series J | 0.443750 | - May 24, 2003 | 25.00 | May 24, 2003 | November 24, 2003 |
| US\$ Non-cumulative Series K | US 0.393750 | May 24, 2003 | US 25.00 | May 24, 2003 | November 24, 2003 |
| Non-cumulative Series N | 0.293750 | August 24, 2003 | 26.00 | August 24, 2003 | August 24, 2008 |
| Non-cumulative Series O | 0.343750 | August 24, 2004 | 26.00 | August 24, 2004 | Not convertible |
| US\$ Non-cumulative Series P | US 0.359375 | August 24, 2004 | US 26.00 | August 24, 2004 | Not convertible |
| Non-cumulative Series S | 0.38125 | August 24, 2006 | 26.00 | August 24, 2006 | Not convertible |

- (1) Non-cumulative preferential dividends on Series J, K, N, O, P and S are payable quarterly, as and when declared by the Board of Directors, on or about the 24th day of February, May, August and November.
- (2) Subject to the consent of the Superintendent of Financial Institutions Canada and the requirements of the *Bank Act*, we may, on or after the dates specified above, redeem First Preferred Shares. These may be redeemed (i) for cash, in the case of First Preferred Shares Series J and K equal to the redemption price as stated above, in the case of Series N at a price per share of \$26, if redeemed during the 12 months commencing August 24, 2003, and decreasing by \$0.25 each 12-month period thereafter to a price per share of \$25 if redeemed on or after August 24, 2007, and in the case of Series O and P at a price per share of \$26 if redeemed during the 12 months commencing August 24, 2004, and decreasing by \$0.25 each 12-month period thereafter to a price per share of \$25 if redeemed on or after August 24, 2008, and in the case of Series S at a price per share of \$26 if redeemed during the 12 months commencing August 26, 2006, and decreasing by \$0.25 each 12-month period thereafter to a price per share of \$25 if redeemed on or after August 24, 2010, or (ii) by conversion, in the case of Series J and K into that number of common shares determined by dividing the then-applicable redemption price by the greater of \$2.50 and 95% of the weighted average trading price of common shares at such time.
- (3) Subject to the consent of the Superintendent of Financial Institutions Canada and the requirements of the *Bank Act*, we may purchase First Preferred Shares for cancellation at a purchase price, in the case of the Series J and K not exceeding the then-applicable redemption price specified above plus all declared and unpaid dividends, and, in the case of the Series N, O, P and S at the lowest price or prices at which, in the opinion of the Board of Directors, such shares are obtainable.
- (4) Subject to the approval of the Toronto Stock Exchange, we may, on or after the dates specified above, convert First Preferred Shares Series N, O, P and S into our common shares. First Preferred Shares may be converted into that number of common shares determined by dividing the then-applicable redemption price by the greater of \$2.50 and 95% of the weighted average trading price of common shares at such time.
- (5) Subject to our right to redeem or to find substitute purchasers, the holder may, on or after the dates specified above, convert First Preferred Shares into our common shares. Series J, K and N may be converted, quarterly, into that number of common shares determined by dividing the then-applicable redemption price by the greater of \$2.50 and 95% of the weighted average trading price of common shares at such time.

Restrictions on the payment of dividends

We are prohibited by the *Bank Act* (Canada) from declaring any dividends on our preferred or common shares when we are, or would be placed as a result of the declaration, in contravention of the capital adequacy and liquidity regulations or any regulatory directives issued under the act. We may not pay dividends on our common shares at any time unless all dividends to which preferred shareholders are then entitled have been declared and paid or set apart for payment.

In addition, we may not declare or pay a dividend without the approval of the Superintendent of Financial Institutions Canada (OSFI) if, on the day the dividend is declared, the total of all dividends in that year would exceed the aggregate of our net income up to that day and of our retained net income for the preceding two years.

We have agreed that if RBC Capital Trust (a closed-end trust, which is a subsidiary) fails to pay any required distribution on its capital trust securities, we will not declare dividends of any kind on any of our preferred or common shares.

Currently, these limitations do not restrict the payment of dividends on our preferred or common shares.

Regulatory capital

We are subject to the regulatory capital requirements defined by OSFI, which includes the use of Canadian GAAP. Two measures of capital strength established by OSFI, based on standards issued by the Bank for International Settlements (BIS), are risk-adjusted capital ratios and the assets-to-capital multiple.

OSFI requires Canadian banks to maintain a minimum Tier 1 and Total capital ratio of 4% and 8%, respectively. However, OSFI has also formally established risk-based capital targets for deposit-taking institutions in Canada. These targets are a Tier 1 capital ratio of at least 7% and a Total capital ratio of at least 10%. At October 31, 2002, our Tier 1 and Total capital ratios were 9.3% and 12.7%, respectively (2001 – 8.7% and 11.8%, respectively).

In the evaluation of our assets-to-capital multiple, OSFI specifies that total assets, including specified off-balance sheet financial instruments, should be no greater than 23 times Total capital. At October 31, 2002, our assets-to-capital multiple was 17.3 times (2001 – 17.2 times).

Using guidelines issued by the Board of Governors of the Federal Reserve System in the United States and U.S. GAAP financial information, our Tier 1 and Total capital ratios at October 31, 2002, were 8.5% and 11.9%, respectively (2001 – 8.1% and 11.2%, respectively).

Other

In 2000, we entered into an agreement with a AAA rated reinsurer, which requires the reinsurer to purchase up to \$200 million of non-cumulative first preferred shares at the October 27, 2000 market price should the general allowance for credit losses (allocated general and unallocated) be drawn down below a certain level. During the year, the reinsurer was downgraded from AAA. Based on this development and an internal review by management, the agreement was not renewed.

NOTE 14 Income taxes

| | 2002 | 2001 | 2000 |
|--|-----------------|---------------|-----------------|
| Provision for income tax in income | | | |
| Current | | | |
| Canada – Federal | \$ 681 | \$ 827 | \$ 799 |
| Provincial | 265 | 354 | 349 |
| International | 155 | 103 | 258 |
| | 1,101 | 1,284 | 1,406 |
| Deferred | | | |
| Canada – Federal | 205 | 22 | 38 |
| Provincial | 70 | 3 | 9 |
| International | 39 | 41 | (41) |
| | 314 | 66 | 6 |
| | 1,415 | 1,350 | 1,412 |
| Income tax expense (benefit) in shareholders' equity | | | |
| Unrealized gains and losses on available for sale securities, net of hedging activities | (4) | 221 | 20 |
| Unrealized foreign currency translation gains and losses, net of hedging activities | 100 | (487) | (37) |
| Gains and losses on derivatives designated as cash flow hedges | 30 | (173) | – |
| Stock appreciation rights | 22 | – | – |
| Additional pension obligation | (155) | (12) | – |
| | (7) | (451) | (17) |
| Total income taxes | \$ 1,408 | \$ 899 | \$ 1,395 |

Deferred income taxes (temporary differences)

| | 2002 | 2001 | 2000 |
|---|-----------------|-----------------|-----------------|
| Deferred income tax asset ⁽¹⁾ | | | |
| Allowance for credit losses | \$ 512 | \$ 582 | \$ 514 |
| Deferred compensation | 339 | 190 | 78 |
| Pension related | 210 | 105 | 44 |
| Tax loss carryforwards | 22 | 84 | 72 |
| Premises and equipment | – | – | 83 |
| Deferred income | 60 | 61 | 152 |
| Other | 259 | 399 | 223 |
| | 1,402 | 1,421 | 1,166 |
| Deferred income tax liability | | | |
| Premises and equipment | (9) | (91) | – |
| Deferred expense | (240) | (149) | (86) |
| Other | (150) | (134) | (77) |
| | (399) | (374) | (163) |
| Net deferred income tax asset | \$ 1,003 | \$ 1,047 | \$ 1,003 |

(1) We have determined that it is more likely than not that the deferred income tax asset will be realized through a combination of future reversals of temporary differences and taxable income.

Reconciliation to statutory tax rate

| | 2002 | | 2001 | | 2000 | |
|--|----------|-------|----------|-------|----------|-------|
| Income taxes at Canadian statutory tax rate | \$ 1,702 | 38.5% | \$ 1,615 | 41.5% | \$ 1,558 | 42.8% |
| Increase (decrease) in income taxes resulting from | | | | | | |
| Lower average tax rate applicable to subsidiaries | (276) | (6.2) | (253) | (6.5) | (303) | (8.3) |
| Tax-exempt income from securities | (7) | (.2) | (7) | (.2) | (7) | (.2) |
| Tax rate change | 33 | .7 | 79 | 2.0 | 20 | .5 |
| Other | (37) | (.8) | (84) | (2.1) | 144 | 4.0 |
| Income taxes reported in income/effective tax rate | \$ 1,415 | 32.0% | \$ 1,350 | 34.7% | \$ 1,412 | 38.8% |

International earnings of certain subsidiaries would be taxed only upon their repatriation to Canada. We have not recognized a deferred tax liability for these undistributed earnings as we do not currently expect them to be repatriated. Taxes that would be payable if all foreign subsidiaries'

accumulated unremitted earnings were repatriated are estimated at \$841 million as at October 31, 2002 (2001 – \$772 million; 2000 – \$737 million).

NOTE 15 Pensions and other postretirement benefits

We sponsor a number of defined benefit and defined contribution plans providing pension and other postretirement benefits to eligible employees.

The following tables present information related to our benefit plans, including amounts recorded on the Consolidated balance sheet and the components of net benefit expense:

Plan assets, benefit obligation and funded status

| | Pension plans (1) | | Other postretirement plans (2) | |
|--|-------------------|----------|--------------------------------|----------|
| | 2002 | 2001 | 2002 | 2001 |
| Change in fair value of plan assets (3) | | | | |
| Fair value of plan assets, October 1 | \$ 4,049 | \$ 4,519 | \$ 1 | \$ 67 |
| Actual return on plan assets | (133) | (476) | – | 7 |
| Company contributions | 99 | 20 | 23 | 21 |
| Plan participant contributions | 19 | 18 | 1 | – |
| Benefits paid | (258) | (251) | (25) | (22) |
| Plan settlements | (52) | – | – | (72) |
| Business acquisitions | – | 63 | – | – |
| Change in foreign currency exchange rate | 17 | 12 | – | – |
| Transfers from other plans | 6 | 144 | – | – |
| Fair value of plan assets, September 30 | \$ 3,747 | \$ 4,049 | \$ – | \$ 1 |
| Change in benefit obligation | | | | |
| Benefit obligation, October 1 | \$ 4,044 | \$ 3,710 | \$ 693 | \$ 609 |
| Service cost | 113 | 104 | 22 | 64 |
| Interest cost | 297 | 268 | 51 | 49 |
| Plan participant contributions | 19 | 18 | 1 | – |
| Actuarial loss | 280 | 55 | 318 | 19 |
| Benefits paid | (258) | (251) | (25) | (22) |
| Transfers from other plans | 3 | – | – | – |
| Plan amendments and curtailments | 59 | 31 | 7 | – |
| Plan settlements | – | – | – | (72) |
| Business acquisitions | 2 | 117 | – | 35 |
| Change in foreign currency exchange rate | 31 | (9) | – | – |
| Changes in assumptions | – | 1 | – | 11 |
| Benefit obligation, September 30 | \$ 4,590 | \$ 4,044 | \$ 1,067 | \$ 693 |
| Funded status | | | | |
| (Deficit) excess of plan assets over benefit obligation | \$ (843) | \$ 5 | \$ (1,067) | \$ (692) |
| Unrecognized net actuarial loss | 792 | 32 | 360 | 42 |
| Unrecognized transition (asset) obligation | (26) | (24) | 190 | 207 |
| Unrecognized prior service cost | 211 | 205 | 13 | 10 |
| Contributions between September 30 and October 31 | 222 | – | 3 | – |
| Other | (1) | (48) | 1 | 1 |
| Net amount recognized as at October 31 | \$ 355 | \$ 170 | \$ (500) | \$ (432) |
| Amounts recognized in the Consolidated balance sheet consist of: | | | | |
| Prepaid pension benefit cost | \$ 109 | \$ 366 | | |
| Accrued pension benefit expense | (419) | (282) | | |
| Intangible asset | 205 | 57 | | |
| Accumulated other comprehensive income | 460 | 29 | | |
| Net amount recognized as at October 31 | \$ 355 | \$ 170 | | |
| Weighted average assumptions | | | | |
| Discount rate | 6.75% | 7.00% | 7.00% | 7.25% |
| Assumed long-term rate of return on plan assets | 7.00% | 7.00% | 4.75% | 4.75% |
| Rate of increase in future compensation | 4.00% | 4.40% | 4.40% | 4.40% |

Pension benefit expense (4)

| | 2002 | 2001 | 2000 |
|--------------------------------------|--------|--------|-------|
| Service cost | \$ 113 | \$ 104 | \$ 98 |
| Interest cost | 297 | 268 | 254 |
| Expected return on plan assets | (300) | (306) | (291) |
| Amortization of transition asset | (2) | (2) | (2) |
| Amortization of prior service cost | 32 | 17 | 22 |
| Recognized net actuarial gain | (27) | (45) | (41) |
| Settlement loss | 52 | – | – |
| Other | (45) | (14) | 19 |
| Defined benefit pension expense | 120 | 22 | 59 |
| Defined contribution pension expense | 61 | 30 | 6 |
| Pension benefit expense | \$ 181 | \$ 52 | \$ 65 |

Other postretirement benefit expense (2)

| | 2002 | 2001 | 2000 |
|---------------------------------------|-------|--------|-------|
| Service cost | \$ 22 | \$ 64 | \$ 17 |
| Interest cost | 51 | 49 | 42 |
| Expected return on plan assets | – | (1) | (3) |
| Amortization of transition obligation | 17 | 17 | 17 |
| Other | 2 | 2 | – |
| Other postretirement benefit expense | \$ 92 | \$ 131 | \$ 73 |

2002 sensitivity of key assumptions

| | Change in obligation | Change in expense |
|---|----------------------|-------------------|
| Pensions | | |
| Impact of .25% change in discount rate assumption | \$ 126 | \$ 16 |
| Impact of .25% change in rate of increase in future compensation assumption | 29 | 2 |
| Impact of .25% change in the long-term rate of return on plan assets assumption | | 10 |
| Postretirement | | |
| Impact of .25% change in discount rate assumption | \$ 48 | \$ 3 |
| Impact of .25% change in rate of increase in future compensation assumption | 4 | 1 |

(1) Included in these amounts are \$3,239 million (2001 – \$266 million) of plan assets and \$4,131 million (2001 – \$567 million) of benefit obligations for plans that are not fully funded.

(2) Includes postretirement health, dental and life insurance. The assumed health care cost trend rates for the next year used to measure the expected cost of benefits covered for the postretirement health and life plans were 8% for medical and 5% for dental, decreasing to an ultimate rate of 4% in 2009. A one percentage point increase in assumed health care cost trend rates would have increased the service and interest costs and obligation by \$12 million and \$142 million, respectively. A one percentage point decrease in assumed health care cost trends would have lowered the service and interest costs and the obligation by \$8 million and \$112 million, respectively.

(3) Plan assets includes 818,597 (2001 – 886,384) of Royal Bank common shares having a fair value of \$43 million (2001 – \$43 million). In addition, dividends amounting to \$1 million (2001 – \$1 million) were received on Royal Bank common shares held in the plan assets during the year.

(4) Discount rate assumption of 7.00% (2001 – 7.00%; 2000 – 7.25%) was used to determine pension benefit expense.

NOTE 16 Stock-based compensation**Stock option plans**

We have two stock option plans – one for certain key employees and one for non-employee directors. Under these plans, options are periodically granted to purchase common shares at prices not less than the market price of such shares on the day of grant. The options vest over a 4-year period for employees and immediately for directors and are exercisable for a period not exceeding 10 years from the grant date.

For options issued prior to October 31, 2002 that were not accompanied by tandem stock appreciation rights (SARs), no compensation expense was recognized as the option's exercise price was not less than the market price of the underlying stock on the day of grant. When the options are exercised, the proceeds received are credited to common shares.

Between November 29, 1999 and June 5, 2001, grants of options under the employee stock option plan were accompanied by tandem SARs. With SARs, participants could choose to exercise a SAR instead of the

corresponding option. In such cases, the participants received a cash payment equal to the difference between the closing price of common shares on the day immediately preceding the day of exercise and the exercise price of the option.

Compensation expense for SARs is recognized using estimates based on past experience, of participants exercising SARs rather than the corresponding options. The compensation expense for these grants, which is amortized over the associated option's vesting period, was \$27 million for the year ended October 31, 2002 (2001 – \$23 million; 2000 – \$52 million).

During the last quarter of 2002, certain executive participants voluntarily renounced their SARs while retaining the corresponding options. At the time of renouncement, the compensation cost was fixed and the accrued liability of \$47 million was transferred to equity.

Stock options

| | 2002 | | 2001 | | 2000 | |
|----------------------------------|--------------------------|---------------------------------|--------------------------|---------------------------------|--------------------------|---------------------------------|
| | Number of options (000s) | Weighted average exercise price | Number of options (000s) | Weighted average exercise price | Number of options (000s) | Weighted average exercise price |
| Outstanding at beginning of year | 30,158 | \$ 36.84 | 25,880 | \$ 33.61 | 20,966 | \$ 32.42 |
| Granted | 4,215 | 49.12 | 7,949 | 44.46 | 8,286 | 33.09 |
| Exercised – Common shares | (5,211) | 32.07 | (2,819) | 28.77 | (2,700) | 22.05 |
| – SARs | (291) | 34.01 | (259) | 33.55 | – | – |
| Cancelled | (392) | 38.37 | (593) | 37.82 | (672) | 36.10 |
| Outstanding at end of year | 28,479 | \$ 39.54 | 30,158 | \$ 36.84 | 25,880 | \$ 33.61 |
| Exercisable at end of year | 14,050 | \$ 36.07 | 12,895 | \$ 32.62 | 8,881 | \$ 30.29 |
| Available for grant | 16,105 | | 20,289 | | 25,849 | |

Range of exercise prices

| | Options outstanding | | | Options exercisable | |
|-----------------|---------------------------|---------------------------------|---|---------------------------|---------------------------------|
| | Number outstanding (000s) | Weighted average exercise price | Weighted average remaining contractual life | Number exercisable (000s) | Weighted average exercise price |
| \$14.46–\$15.68 | 587 | \$ 15.57 | 3.9 | 587 | \$ 15.57 |
| \$24.80–\$28.25 | 2,816 | 26.19 | 6.9 | 2,401 | 25.85 |
| \$30.00–\$39.64 | 15,175 | 36.68 | 7.1 | 9,595 | 37.90 |
| \$43.59–\$52.19 | 9,901 | 49.15 | 9.4 | 1,467 | 49.04 |
| Total | 28,479 | \$ 39.54 | 7.8 | 14,050 | \$ 36.07 |

Fair value method

FAS 123, *Accounting for Stock-Based Compensation*, recommends the recognition of an expense for option awards using the fair value method of accounting. It permits the use of the intrinsic value based method (APB 25, *Accounting for Stock Issued to Employees*), provided pro forma disclosures of net income and earnings per share applying the fair value method are made. For options with SARs attached, FAS 123 recommends the recognition of an intrinsic value based expense for the entire

award. We will be adopting the recommendations of FAS 123 prospectively for new awards granted after November 1, 2002. The impact is an estimated charge to earnings of \$6 million for the year ended October 31, 2003.

We have provided pro forma disclosures, which demonstrate the effect as if we had adopted the recommended recognition provisions of FAS 123 in 2002, 2001 and 2000 as indicated below:

Pro forma net income and earnings per share

| | | As reported | | | Pro forma (1) | | |
|----------------------------|----------|-------------|----------|----------|---------------|----------|--|
| | 2002 | 2001 | 2000 | 2002 | 2001 | 2000 | |
| Net income | \$ 2,898 | \$ 2,435 | \$ 2,208 | \$ 2,856 | \$ 2,399 | \$ 2,164 | |
| Earnings per share | 4.16 | 3.58 | 3.42 | 4.10 | 3.53 | 3.35 | |
| Diluted earnings per share | 4.12 | 3.55 | 3.40 | 4.07 | 3.50 | 3.34 | |

(1) Compensation expense under the fair value based method is recognized over the vesting period of the related stock options. Accordingly, the pro forma results of applying this method may not be indicative of future amounts.

In determining the pro forma disclosures above, the fair value of options granted during 2002 was estimated on the date of grant using an option pricing model with the following assumptions: (i) risk-free interest rate of 4.89% (2001 – 5.86%; 2000 – 6.04%), (ii) expected option life of

6 years (2001, 2000 – 10 years), (iii) expected volatility of 20% (2001 – 24%; 2000 – 22%) and (iv) expected dividends of 2.9% (2001 – 2.67%; 2000 – 2.60%). The fair value of each option granted was \$10.02 (2001 – \$14.78; 2000 – \$10.26).

NOTE 16 Stock-based compensation (continued)**Employee share ownership plans**

We offer many employees an opportunity to own stock through RBC savings and share ownership plans. Under these plans, the employee can generally contribute between 1% and 10% of their annual salary or benefit base for commissioned employees. For each contribution between 1% and 6%, we will match 50% of the employee contributions in common shares. For the RBC Dominion Securities Savings Plan our maximum annual contribution is \$4,500 per employee. For the RBC UK Share Incentive Plan our maximum annual contribution is £1,500 per employee. We contributed \$49 million (2001 – \$47 million; 2000 – \$45 million), under the terms of these plans, towards the purchase of common shares. As at October 31, 2002, an aggregate of 17,397,119 common shares were held under these plans.

Deferred share and other plans

We offer deferred share unit plans to executives and non-employee directors. Under these plans, each executive or director may choose to receive all or a percentage of their annual incentive bonus or directors fee in the form of deferred share units (DSUs). The executives or directors must elect to participate in the plan prior to the beginning of the fiscal year. DSUs earn dividend equivalents in the form of additional DSUs at the same rate as dividends on common shares. The participant is not allowed to convert the DSUs until retirement, permanent disability or termination of employment/directorship. The cash value of the DSUs is equivalent to the market value of common shares when conversion takes place. The value of the DSUs as at October 31, 2002, was \$73 million (2001 – \$52 million; 2000 – \$26 million). The share appreciation and dividend-related compensation expense recorded for the year ended October 31, 2002, in respect of these plans was \$16 million (2001 – \$8 million; 2000 – \$7 million).

We have a deferred bonus plan for certain key employees within RBC Capital Markets. Under this plan, a percentage of each employee's annual incentive bonus is deferred and accumulates dividend equivalents at the same rate as dividends on common shares. The employee will receive the deferred bonus in equal amounts paid within 90 days of the following 3 year-end dates. The value of the deferred bonus paid will be equivalent to the original deferred bonus adjusted for dividends and changes in the market value of common shares at the time the bonus is paid. The value of the deferred bonus as at October 31, 2002, was \$187 million (2001 – \$128 million; 2000 – \$89 million). The share appreciation and dividend-related compensation expense for the year ended October 31, 2002 in respect of this plan was \$20 million (2001 – \$5 million recovery; 2000 – \$10 million).

We offer deferred share plans to certain key employees within RBC Investments with various vesting periods up to a maximum of five years. Awards under some of these plans may be deferred in the form of common shares, which are held in trust, or DSUs. The participant is not allowed to convert the DSU until retirement, permanent disability, or termination of employment. The cash value of DSUs is equivalent to the market value of common shares when conversion takes place. Certain plans award share units that track the value of common shares with payout in cash at the end of a maximum five-year term. The value of

deferred shares held in trust as at October 31, 2002, was \$34 million (2001 – \$14 million). The value of the various share units as at October 31, 2002, was \$10 million (2001 – \$4 million). The stock-based compensation expense recorded for the year ended October 31, 2002, in respect of these plans, was \$32 million (2001 – \$16 million; 2000 – \$14 million).

We offer a performance deferred share plan to certain key employees. The performance deferred share award is made up of 50% regular shares and 50% performance shares all of which vest at the end of 3 years. At the time the shares vest, the performance shares can be increased or decreased by 50% depending on our total shareholder return compared to 15 North American financial institutions. Compensation expense of \$11 million was recognized for the year ended October 31, 2002 in respect of this award. The value of common shares held in trust as at October 31, 2002 was \$34 million.

We offer a mid-term compensation plan to certain senior executive officers. Awards under this program are converted into share units equivalent to common shares. The share units vest over a three-year period in equal installments of one-third per year. The units have a value equal to the market value of common shares on each vesting date and are paid in either cash or common shares at our option. The value of the share units as at October 31, 2002 was \$16 million (2001 – \$21 million). The compensation expense recorded for the year ended October 31, 2002 in respect of this plan was \$12 million (2001 – \$8 million).

Dain Rauscher maintains a non-qualified deferred compensation plan for key employees under an arrangement called the wealth accumulation plan. This plan allows eligible employees to make deferrals of their annual income and allocate the deferrals among various fund choices, which include an RBC share unit fund that tracks the value of our common shares. Certain deferrals may also be eligible for matching contributions from us. All matching contributions are allocated to the RBC share unit fund. The compensation expense recorded for the year ended October 31, 2002, in respect of the matching contributions, was \$12 million (2001 – \$7 million). The value of the RBC share units held under the plan as at October 31, 2002 was \$70 million (2001 – \$7 million).

For other stock-based plans, compensation expense of \$19 million was recognized for the year ended October 31, 2002 (2001 – \$14 million; 2000 – \$1 million). The value of the share units and shares held under these plans as at October 31, 2002 was \$10 million (2001 – \$3 million; 2000 – \$1 million).

Retention plan

On the acquisition of Dain Rauscher, certain key employees of Dain Rauscher were offered retention units awards totalling \$318 million in award value to be paid out evenly over expected service periods of between three and four years. Payments to participants of the plan are based on the market value of common shares on the vesting date. The compensation expense recorded for the year ended October 31, 2002 in respect of this plan was \$92 million (2001 – \$143 million). The liability under this plan was \$151 million as at October 31, 2002 (2001 – \$135 million).

NOTE 17 Earnings per share

| | 2002 | 2001 | 2000 |
|--|----------|----------|----------|
| Earnings per share | | | |
| Net income | \$ 2,898 | \$ 2,435 | \$ 2,208 |
| Preferred share dividends | (98) | (135) | (134) |
| Net income available to common shareholders | \$ 2,800 | \$ 2,300 | \$ 2,074 |
| Average number of common shares (in thousands) | 672,571 | 641,516 | 606,389 |
| | \$ 4.16 | \$ 3.58 | \$ 3.42 |
| Diluted earnings per share | | | |
| Net income available to common shareholders | \$ 2,800 | \$ 2,300 | \$ 2,074 |
| Effect of assumed conversions (1) | — | 1 | 2 |
| Net income adjusted for diluted computation | \$ 2,800 | \$ 2,301 | \$ 2,076 |
| Average number of common shares (in thousands) | 672,571 | 641,516 | 606,389 |
| Convertible Class B and C shares (1) | 14 | 363 | 736 |
| Stock options (2) | 6,568 | 5,337 | 2,740 |
| Average number of diluted common shares (in thousands) | 679,153 | 647,216 | 609,865 |
| | \$ 4.12 | \$ 3.55 | \$ 3.40 |

(1) The convertible shares included the Class B and C shares issued by our wholly owned subsidiary Royal Bank DS Holding Inc., on the acquisition of Richardson Greenshields Limited on November 1, 1996. The outstanding Class B shares were all exchanged into Royal Bank of Canada common shares in 2001 and the remaining Class C shares were exchanged for common shares on November 9, 2001. The price of the Class C shares was determined based on our average common share price during the 20 days prior to the date the exchange was made. During the year we exchanged nil (2001 – 36,527; 2000 – 4,701) Class B shares and 1,846,897 (2001 – 77,956; 2000 – 8,008,712) Class C shares for 318,154 (2001 – 13,621; 2000 – 1,667,334) common shares.

(2) The dilutive effect of stock options was calculated using the treasury stock method. This method calculates the number of incremental shares by assuming the outstanding stock options are (i) exercised and (ii) then reduced by the number of shares assumed to be repurchased from the issuance proceeds, using the average market price of our common shares for the period. Excluded from the calculation of diluted earnings per share were average options outstanding of 9,761 with an exercise price of \$53.76 (2001 – 7,862 at \$50.72; 1,956 at \$49.03; 2000 – 6,153,507 at \$39.64; 6,589,464 at \$39.01; 2,639 at \$38.22; and 393 at \$43.59) as the options' exercise price was greater than the average market price of our common shares.

NOTE 18 Commitments and contingencies**Financial instruments with contractual amounts representing credit risk**

The primary purpose of these commitments is to ensure that funds are available to a client as required. Our policy for requiring collateral security with respect to these instruments and the types of collateral security held is generally the same as for loans.

Guarantees and standby letters of credit, which represent irrevocable assurances that we will make payments in the event that a client cannot meet its obligations to third parties, carry the same credit risk as loans.

Documentary and commercial letters of credit, which are written undertakings by us on behalf of a client authorizing a third party to draw drafts on us up to a stipulated amount under specific terms and conditions, are collateralized by the underlying shipment of goods to which they relate.

In securities lending transactions, we act as an agent for the owner of a security, who agrees to lend the security to a borrower for a fee, under the terms of a pre-arranged contract. The borrower must fully collateralize the security loan at all times.

Commitments to extend credit represent unused portions of authorizations to extend credit in the form of loans, bankers' acceptances, guarantees or letters of credit.

Uncommitted amounts represent an amount for which we retain the option to extend credit to a borrower.

A note issuance facility represents an underwriting agreement that enables a borrower to issue short-term debt securities. A revolving underwriting facility represents a renewable note issuance facility that can be accessed for a specified period of time.

Financial instruments with contractual amounts representing credit risk

| | 2002 | 2001 |
|---|------------|------------|
| Guarantees and standby letters of credit | \$ 13,610 | \$ 13,391 |
| Documentary and commercial letters of credit | 772 | 750 |
| Securities lending | 23,967 | 21,377 |
| Commitments to extend credit | | |
| Original term to maturity of 1 year or less | 40,931 | 44,179 |
| Original term to maturity of more than 1 year | 34,115 | 39,960 |
| Uncommitted amounts | 45,978 | 53,750 |
| Note issuance/revolving underwriting facilities | 23 | 132 |
| | \$ 159,396 | \$ 173,539 |

NOTE 18 Commitments and contingencies (continued)**Lease commitments**

Minimum future rental commitments for premises and equipment under long-term non-cancellable leases for the next five years and thereafter are shown below.

Lease commitments

| | |
|--------------|-----------------|
| 2003 | \$ 364 |
| 2004 | 330 |
| 2005 | 300 |
| 2006 | 267 |
| 2007 | 203 |
| Thereafter | 754 |
| Total | \$ 2,218 |

Litigation

On June 21, 2002, a week before it was due to pay Royal Bank of Canada US\$517 million plus interest under the terms of a total return swap, which is recorded in Other assets, Cooperatieve Centrale Raiffeisen-Boerenleenbank B.A. (Rabobank) initiated an action against us in New York state court in an effort to nullify its obligation under the swap. On June 24, 2002, we instituted proceedings against Rabobank in the High Court in London, alleging that Rabobank had repudiated its obligation under the swap. On July 31, 2002, we filed a motion to dismiss

or stay Rabobank's New York lawsuit. Rabobank filed, on September 27, 2002, an application to stay our claim with the High Court in London. Both our motion to stay or dismiss and Rabobank's application to stay are proceeding and the matter of forum is expected to be considered by both courts in the near future. Management expects to recover this amount in its entirety and accordingly a provision for loss has not been recorded.

Various other legal proceedings are pending that challenge certain of our practices or actions. Many of these proceedings are loan-related and are in reaction to steps taken by us and our subsidiaries to collect delinquent loans and enforce rights in collateral securing such loans. Management considers that the aggregate liability resulting from these proceedings will not be material.

Pledged assets

In the ordinary course of business we accept collateral, generally under reverse repurchase and securities borrowing agreements. The fair value of collateral accepted that can be sold or repledged by us totalled \$55.9 billion (2001 – \$52.9 billion). Of this collateral, \$36.4 billion (2001 – \$41.9 billion) has been sold or repledged, generally as collateral under repurchase agreements or to cover short sales. Details of assets pledged against liabilities, including amounts that cannot be sold or repledged by the secured party, are shown below:

Pledged assets

| | 2002 | 2001 |
|--|------------------|------------------|
| Assets pledged to: | \$ | \$ |
| Foreign governments and central banks | 1,418 | 113 |
| Clearing systems, payment systems and depositories | 1,075 | 2,470 |
| Assets pledged in relation to: | | |
| Derivative transactions | 1,828 | 830 |
| Securities borrowing and lending | 19,720 | 16,007 |
| Obligations related to securities sold under repurchase agreements | 21,109 | 20,855 |
| Other | 3,389 | 6,095 |
| Total | \$ 48,539 | \$ 46,370 |

NOTE 19 Derivative financial instruments

Derivative financial instruments are financial contracts whose value is derived from an underlying interest rate, foreign exchange rate, equity or commodity instrument or index.

Derivative product types

We use the following derivative financial instruments for both trading and non-trading purposes.

Swaps are transactions in which two parties exchange cash flows on a specified notional amount for a predetermined period. For interest rate swaps, fixed and floating interest payments are exchanged based on a notional amount. Cross currency swaps involve the exchange of fixed or floating interest payments in one currency for the receipt of fixed or floating interest payments in another currency. Cross currency interest rate swaps involve the exchange of both interest and principal amounts in two different currencies.

Forwards and futures are contractual obligations to buy or sell a financial instrument on a future date at a specified price. Forward contracts are effectively tailor-made agreements that are transacted between counterparties in the over-the-counter market, whereas futures are standardized contracts that are transacted on regulated exchanges.

Options are contractual agreements under which the seller (writer) grants the purchaser the right, but not the obligation, either to buy (call option) or sell (put option), by or at a set date, a specified amount of

a financial instrument at a predetermined price. The seller receives a premium from the purchaser for this right.

Credit derivatives are contracts whose redemption value is linked to specified credit related events, such as bankruptcy, credit downgrade, non-payment or default. Examples of credit derivatives include credit default swaps, total return swaps and credit default baskets.

Derivatives held or issued for trading purposes

Most of our derivative transactions relate to sales and trading activities. Sales activities include the structuring and marketing of derivative products to clients to enable them to transfer, modify or reduce current or expected risks. Trading involves market-making, positioning and arbitrage activities. Market-making involves quoting bid and offer prices to other market participants with the intention of generating revenues based on spread and volume. Positioning involves managing market risk positions with the expectation of profiting from favourable movements in prices, rates or indices. Arbitrage activities involve identifying and profiting from price differentials between markets and products. We do not deal, to any significant extent, in leveraged derivative transactions. These transactions contain a multiplier which, for any given change in market prices, could cause the change in the transaction's fair value to be significantly different from the change in fair value that would occur for a similar derivative without the multiplier.

Derivatives held or issued for non-trading purposes

We also use derivatives in connection with our own asset/liability management activities, which include hedging and investment activities.

Interest rate swaps are used to adjust exposure to interest rate risk by modifying the repricing or maturity characteristics of existing and/or anticipated assets and liabilities. Purchased interest rate options are used to hedge redeemable deposits and other options embedded in consumer products. Written options are used in our asset/liability management activities when specifically linked to a purchased option in the form of a collar. We use credit derivatives to manage our credit exposures and for risk diversification in our lending portfolio.

Our overall interest rate risk management objective is to minimize significant unplanned fluctuations in earnings and cash flows caused by interest rate volatility. Interest rate fluctuations will either cause assets and liabilities to appreciate or depreciate in market value or cause a variability in cash flows. In a fair value hedge, gains or losses on derivatives that are linked to these assets and liabilities will substantially offset the unrealized appreciation or depreciation. In a cash flow hedge, derivatives linked to the assets and liabilities will reduce the variability of cash flows resulting from interest rate fluctuations.

We may also choose to enter into derivative transactions to economically hedge certain business strategies that do not otherwise qualify for hedge accounting, or where hedge accounting is not considered economically feasible to implement. In such circumstances, volatility from interest rate movements is reflected in Non-interest revenue.

Fair value hedge

For the year ended October 31, 2002, the ineffective portions recognized in Non-interest revenue amounted to a net unrealized gain of \$10 million (2001 – \$11 million loss). All components of each derivative's

change in fair value have been included in the assessment of fair value hedge effectiveness.

We did not hedge any firm commitments for the year ended October 31, 2002.

Cash flow hedge

For the year ended October 31, 2002, a net unrealized loss of \$50 million (2001 – \$190 million, net of FAS 133 transition adjustment), was recorded in Other comprehensive income for the effective portion of changes in fair value of derivatives designated as cash flow hedges. The amounts recognized as Other comprehensive income are reclassified to Net income in the periods in which Net income is affected by the variability in cash flows of the hedged item. A net loss of \$113 million (2001 – nil) was reclassified to Net income during the year. A net loss of \$59 million (2001 – \$81 million) deferred in Accumulated other comprehensive income as at October 31, 2002, is expected to be reclassified to Net income during the next 12 months.

For the year ended October 31, 2002, a net unrealized gain of \$9 million (2001 – \$20 million) was recognized in Non-interest revenue for the ineffective portions of cash flow hedges. All components of each derivative's change in fair value have been included in the assessment of cash flow hedge effectiveness.

We did not hedge any forecasted transactions for the year ended October 31, 2002.

Derivatives – Notional amounts

Notional amounts, which are off-balance sheet, serve as a point of reference for calculating payments and are a common measure of business volume. The following table provides the notional amounts of our derivative transactions by term to maturity.

Notional amount of derivatives by term to maturity ⁽¹⁾

| | Term to maturity | | | | 2002 | | 2001 | |
|---|--------------------|-------------------|-----------------------------|--------------------|--------------------|--------------------|--------------------|--------------------|
| | Within 1 year | 1 to 5 years | Over 5 years ⁽²⁾ | Total | Trading | Other than trading | Trading | Other than trading |
| Over-the-counter (OTC) contracts | | | | | | | | |
| Interest rate contracts | | | | | | | | |
| Forward rate agreements | \$ 184,487 | \$ 14,358 | \$ – | \$ 198,845 | \$ 194,537 | \$ 4,308 | \$ 95,678 | \$ – |
| Swaps | 264,829 | 418,082 | 179,353 | 862,264 | 794,961 | 67,303 | 628,735 | 69,167 |
| Options purchased | 8,193 | 35,623 | 11,477 | 55,293 | 55,289 | 4 | 19,787 | 114 |
| Options written | 9,306 | 34,564 | 12,304 | 56,174 | 56,080 | 94 | 22,177 | – |
| Foreign exchange contracts | | | | | | | | |
| Forward contracts | 507,410 | 33,673 | 3,636 | 544,719 | 522,035 | 22,684 | 528,467 | 17,969 |
| Cross currency swaps | 893 | 3,405 | 5,609 | 9,907 | 9,907 | – | 8,618 | – |
| Cross currency interest rate swaps | 10,286 | 37,315 | 26,547 | 74,148 | 71,050 | 3,098 | 63,405 | 2,796 |
| Options purchased | 53,200 | 3,004 | – | 56,204 | 56,160 | 44 | 48,542 | 612 |
| Options written | 58,594 | 3,242 | – | 61,836 | 61,209 | 627 | 54,133 | – |
| Credit derivatives ⁽³⁾ | 3,625 | 37,333 | 11,193 | 52,151 | 50,928 | 1,223 | 20,952 | 955 |
| Other contracts ⁽⁴⁾ | 9,514 | 5,221 | 7,884 | 22,619 | 22,085 | 534 | 20,170 | 2,643 |
| Exchange-traded contracts | | | | | | | | |
| Interest rate contracts | | | | | | | | |
| Futures – long positions | 19,207 | 7,535 | 19 | 26,761 | 26,761 | – | 20,319 | – |
| Futures – short positions | 31,583 | 5,185 | 25 | 36,793 | 36,500 | 293 | 43,232 | 87 |
| Options purchased | 1,418 | 1 | – | 1,419 | 640 | 779 | 13,352 | – |
| Options written | 2,368 | 2 | – | 2,370 | 2,059 | 311 | 12,079 | – |
| Foreign exchange contracts | | | | | | | | |
| Futures – long positions | 27 | – | – | 27 | 27 | – | 348 | – |
| Futures – short positions | 321 | – | – | 321 | 321 | – | 144 | – |
| Other contracts ⁽⁴⁾ | 18,356 | 455 | – | 18,811 | 18,811 | – | 58,130 | – |
| | \$1,183,617 | \$ 638,998 | \$ 258,047 | \$2,080,662 | \$1,979,360 | \$ 101,302 | \$1,658,268 | \$ 94,343 |

(1) The notional amount of \$5,593 million (2001 – \$1,693 million) of derivatives embedded in financial instruments, certain warrants and loan commitments considered as derivatives are excluded from the amounts in this table.

(2) Includes contracts maturing in over 10 years with a notional value of \$37,322 million (2001 – \$19,637 million). The related gross positive replacement cost is \$1,291 million (2001 – \$950 million).

(3) Comprises credit default swaps, total return swaps and credit default baskets.

(4) Comprises precious metals, commodity and equity-linked derivative contracts.

Derivative-related credit risk

Credit risk from derivative transactions is generated by the potential for the counterparty to default on its contractual obligations when one or more transactions have a positive market value to us. This market value is referred to as replacement cost since it is an estimate of what it would cost to replace transactions at prevailing market rates if a default occurred.

For internal risk management purposes, the credit equivalent amount arising from a derivative transaction is defined as the sum of the replacement cost plus an add-on that is an estimate of the potential change in the market value of the transaction through to maturity. The add-on is determined by statistically based models that project the expected volatility of the variable(s) underlying the derivative, whether interest rate, foreign exchange rate, equity or commodity price. Both the

NOTE 19 Derivative financial instruments (continued)

replacement cost and the add-on are continually re-evaluated over the life of each transaction to ensure that sound credit risk valuations are used. The risk-adjusted amount is determined by applying standard measures of counterparty risk to the credit equivalent amount.

Netting is a technique that can reduce credit exposure from derivatives and is generally facilitated through the use of master netting agreements. The two main categories of netting are close-out netting and settlement netting. Under the close-out netting provision, if the counterparty defaults, we have the right to terminate all transactions covered by the master agreement at the then-prevailing market values and to sum the resulting market values, offsetting negative against positive values, to arrive at a single net amount owed by either the counterparty or us. Under the settlement netting provision, all payments and receipts in the same currency and due on the same day between specified pairs including us and the counterparty units are netted, generating a single payment in each currency, due either by us or the counterparty unit. We actively encourage counterparties to enter into master netting agreements. However, measurement of our credit exposure arising out of derivative transactions is not reduced to reflect the effects of netting unless the enforceability of that netting is supported by appropriate legal analysis as documented in our policy.

To further manage derivative-related counterparty credit exposure, we enter into agreements containing mark-to-market cap provisions with some counterparties. Under such provisions, we have the right to request that the counterparty pay down or collateralize the current market value of its derivatives position with us. The use of collateral does not currently represent a significant credit mitigation technique for us in managing derivative-related credit risk.

We subject our derivative-related credit risks to the same credit approval, limit and monitoring standards that we use for managing other transactions that create credit exposure. This includes evaluation of counterparties as to creditworthiness, and managing the size, diversification and maturity structure of the portfolio. Credit utilization for all products is compared with established limits on a continual basis and is subject to a standard exception reporting process. We utilize a single internal rating system for all credit risk exposure. In most cases, these internal ratings approximate the external risk ratings of public rating agencies. The tables below show replacement cost, credit equivalent and risk-adjusted amounts of our derivatives both before and after the impact of netting. During 2002 and 2001, neither our actual credit losses arising from derivative transactions nor the level of impaired derivative contracts were significant.

Replacement cost of derivative financial instruments by risk rating and by counterparty type (1)

| As at October 31, 2002 | Risk rating (2) | | | | | Counterparty type (3) | | | |
|--|-----------------|-----------|----------|-------------|-----------|-----------------------|------------------|----------|-----------|
| | AAA, AA | A | BBB | BB or lower | Total | Banks | OECD governments | Other | Total |
| Gross positive replacement cost (4) | \$ 15,442 | \$ 11,008 | \$ 3,421 | \$ 1,580 | \$ 31,451 | \$ 21,427 | \$ 2,068 | \$ 7,956 | \$ 31,451 |
| Impact of master netting agreements | (10,638) | (7,208) | (2,142) | (873) | (20,861) | (16,343) | — | (4,518) | (20,861) |
| Replacement cost (after netting agreements) | \$ 4,804 | \$ 3,800 | \$ 1,279 | \$ 707 | \$ 10,590 | \$ 5,084 | \$ 2,068 | \$ 3,438 | \$ 10,590 |
| Replacement cost (after netting agreements) – 2001 | \$ 3,583 | \$ 4,322 | \$ 1,515 | \$ 529 | \$ 9,949 | \$ 3,652 | \$ 1,892 | \$ 4,405 | \$ 9,949 |

- (1) The replacement cost of \$93 million (2001 – \$49 million) of derivatives embedded in financial instruments, certain warrants and loan commitments considered as derivatives are excluded from the amounts in this table.
- (2) Our internal risk ratings for major counterparty types approximate those of public rating agencies. Ratings of AAA, AA, A and BBB represent investment grade ratings and ratings of BB or lower represent non-investment grade ratings.
- (3) Counterparty type is defined in accordance with the capital adequacy requirements of the Superintendent of Financial Institutions Canada.
- (4) Represents the total current replacement value of all outstanding contracts in a gain position, before factoring in the impact of master netting agreements. Exchange-traded instruments are subject to daily margin requirements and are excluded as they are deemed to have no additional credit risk. The fair value of \$194 million (2001 – \$194 million) is excluded at October 31, 2002. Written options are excluded as they represent our obligations and as such do not attract credit risk.

Derivative-related credit risk (1)

| | 2002 | | | 2001 | | |
|--|----------------------|------------------------------|---------------------------|----------------------|------------------------------|---------------------------|
| | Replacement cost (2) | Credit equivalent amount (3) | Risk-adjusted balance (4) | Replacement cost (2) | Credit equivalent amount (3) | Risk-adjusted balance (4) |
| Interest rate contracts | | | | | | |
| Forward rate agreements | \$ 178 | \$ 299 | \$ 64 | \$ 108 | \$ 543 | \$ 114 |
| Swaps | 19,608 | 24,357 | 6,323 | 17,568 | 21,390 | 5,617 |
| Options purchased | 563 | 914 | 258 | 416 | 538 | 123 |
| | 20,349 | 25,570 | 6,645 | 18,092 | 22,471 | 5,854 |
| Foreign exchange contracts | | | | | | |
| Forward contracts | 6,802 | 13,049 | 3,685 | 6,839 | 12,977 | 3,881 |
| Swaps | 1,781 | 6,341 | 1,445 | 1,902 | 5,536 | 1,261 |
| Options purchased | 809 | 1,491 | 439 | 721 | 1,339 | 441 |
| | 9,392 | 20,881 | 5,569 | 9,462 | 19,852 | 5,583 |
| Credit derivatives (5) | 861 | 2,963 | 858 | 87 | 1,249 | 369 |
| Other contracts (6) | 849 | 1,701 | 529 | 1,140 | 2,015 | 617 |
| Derivatives before master netting agreements | 31,451 | 51,115 | 13,601 | 28,781 | 45,587 | 12,423 |
| Impact of master netting agreements | (20,861) | (26,930) | (7,132) | (18,832) | (24,450) | (6,339) |
| Total derivatives after master netting agreements | \$ 10,590 | \$ 24,185 | \$ 6,469 | \$ 9,949 | \$ 21,137 | \$ 6,084 |

- (1) The replacement cost of \$93 million (2001 – \$49 million) of derivatives embedded in financial instruments, certain warrants and loan commitments considered as derivatives are excluded from the amounts in this table.
- (2) Represents the total current replacement value of all outstanding contracts in a gain position, before factoring in the impact of master netting agreements. Exchange-traded instruments are subject to daily margin requirements and are excluded as they are deemed to have no additional credit risk. The fair value of \$194 million (2001 – \$194 million) is excluded at October 31, 2002. Written options are excluded as they represent our obligations and as such do not attract credit risk.
- (3) Consists of (i) the total positive replacement value of all outstanding contracts, and (ii) an amount for potential future credit exposure.
- (4) Using guidelines issued by the Superintendent of Financial Institutions Canada.
- (5) Comprises credit default swaps, total return swaps and credit default baskets.
- (6) Comprises precious metals, commodity and equity-linked derivative contracts.

NOTE 20 Concentrations of credit risk

Concentrations of credit risk exist if a number of clients are engaged in similar activities, or are located in the same geographic region or have comparable economic characteristics such that their ability to meet contractual obligations would be similarly affected by changes in economic,

political or other conditions. Concentrations of credit risk indicate the relative sensitivity of our performance to developments affecting a particular industry or geographic location. The concentrations described below are within limits as established by management.

| 2002 | | | | | | | | | | 2001 | | | | | | | | | |
|--|-----------|-----|---------------|-----|-----------|-----|---------------------|----|-----------|-----------|-----|---------------|-----|-----------|-----|---------------------|----|-----------|--|
| | Canada | % | United States | % | Europe | % | Other International | % | Total | Canada | % | United States | % | Europe | % | Other International | % | Total | |
| On-balance sheet assets (1) | \$158,059 | 73% | \$ 32,450 | 15% | \$ 18,917 | 9% | \$ 5,979 | 3% | \$215,405 | \$164,429 | 76% | \$ 29,612 | 14% | \$ 17,124 | 8% | \$ 5,805 | 2% | \$216,970 | |
| Off-balance sheet credit instruments (2) | | | | | | | | | | | | | | | | | | | |
| Committed and uncommitted (3) | \$ 60,397 | 50% | \$ 45,573 | 38% | \$ 13,863 | 11% | \$ 1,191 | 1% | \$121,024 | \$ 76,832 | 56% | \$ 43,508 | 32% | \$ 14,465 | 10% | \$ 3,084 | 2% | \$137,889 | |
| Other | 23,266 | 61 | 10,723 | 28 | 4,235 | 11 | 148 | - | 38,372 | 20,990 | 59 | 9,893 | 28 | 4,436 | 12 | 331 | 1 | 35,650 | |
| | \$ 83,663 | 53% | \$ 56,296 | 35% | \$ 18,098 | 11% | \$ 1,339 | 1% | \$159,396 | \$ 97,822 | 56% | \$ 53,401 | 31% | \$ 18,901 | 11% | \$ 3,415 | 2% | \$173,539 | |
| Derivatives before master netting agreements (4), (5), (6) | \$ 7,734 | 25% | \$ 9,887 | 31% | \$ 12,232 | 39% | \$ 1,598 | 5% | \$ 31,451 | \$ 6,899 | 24% | \$ 9,154 | 32% | \$ 11,741 | 41% | \$ 987 | 3% | \$ 28,781 | |

- (1) Includes assets purchased under reverse repurchase agreements, loans and customers' liability under acceptances. The largest concentrations in Canada are Ontario at 38% (2001 – 39%) and British Columbia at 11% (2001 – 12%). No industry accounts for more than 10% of total on-balance sheet credit instruments.
- (2) Represents financial instruments with contractual amounts representing credit risk.
- (3) Of the commitments to extend credit, the largest industry concentration relates to financial institutions at 35% (2001 – 34%), mining and energy at 15% (2001 – 15%), transportation at 8% (2001 – 10%) and manufacturing at 8% (2001 – 10%).
- (4) The largest concentration by counterparty type of this credit exposure is with banks at 68% (2001 – 64%).
- (5) The replacement cost of \$93 million (2001 – \$49 million) of derivatives embedded in financial instruments, certain warrants and loan commitments considered as derivatives are excluded from the amounts in this table.
- (6) Represents the total current replacement value of all outstanding contracts in a gain position, before factoring in the impact of master netting agreements. Exchange-traded instruments are subject to daily margin requirements and are excluded as they are deemed to have no additional credit risk. The fair value of \$194 million (2001 – \$194 million) is excluded at October 31, 2002. Written options are excluded as they represent our obligations and as such do not attract credit risk.

NOTE 21 Estimated fair value of financial instruments

The estimated fair values disclosed below are designed to approximate values at which these instruments could be exchanged in a current transaction between willing parties. However, many of the financial instruments lack an available trading market and therefore, fair values are based on estimates using net present value and other valuation techniques, which are significantly affected by the assumptions used concerning the amount and timing of estimated future cash flows and

discount rates, which reflect varying degrees of risk. Furthermore, due to the use of subjective judgment and uncertainties, the aggregate fair value amounts should not be interpreted as being realizable in an immediate settlement of the instruments.

The estimated fair values disclosed below do not reflect the value of assets and liabilities that are not considered financial instruments such as premises and equipment.

Financial assets and liabilities

| | 2002 | | | 2001 | | |
|--|------------|------------|------------|------------|------------|------------|
| | Book value | Fair value | Difference | Book value | Fair value | Difference |
| Financial assets | | | | | | |
| Cash resources | \$ 21,293 | \$ 21,293 | \$ – | \$ 17,516 | \$ 17,535 | \$ 19 |
| Securities | 95,353 | 95,353 | – | 81,100 | 81,100 | – |
| Assets purchased under reverse repurchase agreements | 35,831 | 35,831 | – | 35,870 | 35,870 | – |
| Loans | 169,320 | 171,546 | 2,226 | 168,899 | 173,263 | 4,364 |
| Other assets | 51,679 | 51,679 | – | 50,668 | 50,668 | – |
| Financial liabilities | | | | | | |
| Deposits | 245,040 | 246,515 | (1,475) | 235,687 | 238,092 | (2,405) |
| Acceptances | 8,051 | 8,051 | – | 9,923 | 9,923 | – |
| Obligations related to securities sold short | 17,990 | 17,990 | – | 16,037 | 16,037 | – |
| Obligations related to assets sold under repurchase agreements | 21,109 | 21,109 | – | 20,864 | 20,864 | – |
| Other liabilities | 61,639 | 61,639 | – | 52,890 | 52,890 | – |
| Subordinated debentures | 6,960 | 6,935 | 25 | 6,861 | 6,845 | 16 |

NOTE 21 Estimated fair value of financial instruments (continued)**Derivatives (1)**

| | 2002 | | | | 2001 | |
|---|---|-----------|---------------------|-----------|---------------------|-----------|
| | Average fair value for the year ended (2) | | Year-end fair value | | Year-end fair value | |
| | Positive | Negative | Positive | Negative | Positive | Negative |
| Held or issued for trading purposes | | | | | | |
| Interest rate contracts | | | | | | |
| Forward rate agreements | \$ 96 | \$ 82 | \$ 178 | \$ 177 | \$ 108 | \$ 79 |
| Swaps | 13,650 | 14,323 | 18,468 | 18,930 | 16,211 | 16,692 |
| Options purchased | 385 | — | 564 | — | 442 | — |
| Options written | — | 325 | — | 474 | — | 352 |
| | 14,131 | 14,730 | 19,210 | 19,581 | 16,761 | 17,123 |
| Foreign exchange contracts | | | | | | |
| Forward contracts | 7,539 | 6,934 | 6,568 | 6,260 | 6,800 | 5,868 |
| Cross currency swaps | 501 | 294 | 504 | 340 | 518 | 315 |
| Cross currency interest rate swaps | 1,462 | 1,853 | 1,109 | 1,678 | 1,309 | 1,975 |
| Options purchased | 827 | — | 809 | — | 715 | — |
| Options written | — | 729 | — | 586 | — | 560 |
| | 10,329 | 9,810 | 8,990 | 8,864 | 9,342 | 8,718 |
| Credit derivatives (3) | 273 | 259 | 822 | 483 | 84 | 79 |
| Other contracts (4) | 1,077 | 2,853 | 1,028 | 3,093 | 1,012 | 2,650 |
| | \$ 25,810 | \$ 27,652 | 30,050 | 32,021 | 27,199 | 28,570 |
| Held or issued for other than trading purposes | | | | | | |
| Interest rate contracts | | | | | | |
| Forward rate agreements | | | — | 49 | — | — |
| Swaps | | | 1,140 | 842 | 1,357 | 1,104 |
| Options purchased | | | 1 | — | — | — |
| Options written | | | — | 13 | — | — |
| | | | 1,141 | 904 | 1,357 | 1,104 |
| Foreign exchange contracts | | | | | | |
| Forward contracts | | | 234 | 94 | 39 | 313 |
| Cross currency interest rate swaps | | | 168 | 24 | 75 | 50 |
| Options purchased | | | — | — | 6 | — |
| Options written | | | — | 3 | — | — |
| | | | 402 | 121 | 120 | 363 |
| Credit derivatives (3) | | | 39 | 8 | 3 | 3 |
| Other contracts (4) | | | 13 | — | 296 | 48 |
| | | | 1,595 | 1,033 | 1,776 | 1,518 |
| Total gross fair values before netting | | | 31,645 | 33,054 | 28,975 | 30,088 |
| Impact of master netting agreements | | | | | | |
| With intent to settle net or simultaneously (5) | | | (12) | (12) | (39) | (39) |
| Without intent to settle net or simultaneously (6) | | | (20,849) | (20,849) | (18,793) | (18,793) |
| Total | | | \$ 10,784 | \$ 12,193 | \$ 10,143 | \$ 11,256 |

(1) The fair value amount of \$93 million (2001 – \$49 million) of derivatives embedded in financial instruments, certain warrants and loan commitments considered as derivatives are excluded from the amounts in this table.

(2) Average fair value amounts are calculated based on monthly balances.

(3) Comprises credit default swaps, total return swaps and credit default baskets.

(4) Comprises precious metals, commodity and equity-linked derivative contracts.

(5) Impact of offsetting credit exposures on contracts where we have both a legally enforceable master netting agreement in place and we intend to settle the contracts on either a net basis or simultaneously.

(6) Additional impact of offsetting credit exposures on contracts where we have a legally enforceable master netting agreement in place but do not intend to settle the contracts on a net basis or simultaneously.

Methodologies and assumptions used to estimate fair values of financial instruments

Loans The fair value of the business and government loans portfolio is based on an assessment of two key risks as appropriate; interest rate risk and credit risk. Fair value is determined under a discounted cash flow methodology using a discount rate based on interest rates currently charged for new loans with similar terms and remaining maturities, adjusted for a credit risk factor, which is reviewed at least annually. Fair value of the consumer loan portfolio is based on a discounted cash flow methodology adjusted principally for prepayment risk. For certain variable rate loans that reprice frequently and loans without a stated maturity, fair values are assumed to be equal to carrying values.

Securities The fair values of securities are provided in the Securities note to the consolidated financial statements (note 5). These are based on quoted market prices, when available. If quoted market prices are not available, fair values are estimated using quoted market prices of similar securities.

Deposits The fair values of fixed rate deposits with a fixed maturity are determined by discounting the expected future cash flows, using market interest rates currently offered for deposits of similar terms and remaining maturities (adjusted for early redemptions where appropriate). The fair values of deposits with no stated maturity or deposits with floating rates are assumed to be equal to their carrying values.

Other assets/liabilities The carrying values of Other assets and Other liabilities approximate their fair values with the exception of amounts relating to derivative financial instruments held or issued for other than trading purposes. The net fair value over book value for these instruments is shown in Other assets.

Subordinated debentures The fair values of subordinated debentures are based on quoted market prices for similar issues, or current rates offered to us for debt of the same remaining maturity.

Financial instruments valued at carrying value Due to their short term nature, the fair value of cash resources, assets purchased under reverse repurchase agreements, customers' liability under acceptances, our liability under acceptances, obligations related to securities sold short and obligations related to assets sold under repurchase agreements is assumed to approximate carrying value.

Derivative financial instruments The fair values of derivative financial instruments are determined using various methodologies. For exchange-traded instruments, fair value is based on quoted market prices, where available. For non-exchange-traded instruments or where no quoted market prices are available, fair value is based on prevailing market rates for instruments with similar characteristics and maturities, net present value analysis or other pricing models as appropriate.

Supplementary information

Consolidated balance sheet

| As at October 31 (C\$ millions) | 2002 | 2001 | 2000 | 1999 | 1998 | 1997 | 1996 | 1995 | 1994 | 1993 | 1992 |
|---|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|
| Assets | | | | | | | | | | | |
| Cash resources | \$ 21,293 | \$ 17,516 | \$ 16,408 | \$ 23,042 | \$ 16,395 | \$ 21,392 | \$ 23,567 | \$ 17,710 | \$ 16,449 | \$ 10,874 | \$ 10,938 |
| Securities | 95,353 | 81,100 | 63,461 | 52,736 | 42,538 | 33,343 | 41,261 | 33,220 | 27,695 | 24,011 | 16,146 |
| Reverse repurchase agreements | 35,831 | 35,870 | 18,303 | 20,272 | 19,907 | 18,642 | 11,446 | 4,591 | 5,259 | 5,304 | 607 |
| Loans | | | | | | | | | | | |
| Residential mortgage | 72,842 | 67,444 | 62,984 | 59,242 | 56,468 | 53,369 | 48,120 | 45,131 | 44,109 | 43,781 | 32,609 |
| Personal | 31,956 | 32,511 | 28,019 | 25,255 | 22,761 | 20,864 | 18,440 | 16,923 | 16,508 | 16,487 | 15,462 |
| Credit card | 4,914 | 4,283 | 4,666 | 2,666 | 1,945 | 2,324 | 3,522 | 3,435 | 3,321 | 3,090 | 2,532 |
| Business and government | 61,811 | 66,939 | 60,515 | 57,630 | 65,598 | 62,837 | 56,138 | 51,500 | 48,748 | 52,062 | 52,502 |
| | 171,523 | 171,177 | 156,184 | 144,793 | 146,772 | 139,394 | 126,220 | 116,989 | 112,686 | 115,420 | 103,105 |
| Allowance for loan losses | (2,203) | (2,278) | (1,871) | (1,884) | (2,026) | (1,769) | (1,875) | (2,003) | (2,559) | (4,255) | (3,575) |
| | 169,320 | 168,899 | 154,313 | 142,909 | 144,746 | 137,625 | 124,345 | 114,986 | 110,127 | 111,165 | 99,530 |
| Other | | | | | | | | | | | |
| Customers' liability under acceptances | 8,051 | 9,923 | 11,628 | 9,257 | 10,620 | 10,561 | 7,423 | 6,300 | 6,205 | 6,302 | 5,737 |
| Derivative-related amounts (1) | 31,250 | 28,642 | 19,334 | 15,151 | 30,413 | 14,776 | 8,598 | 12,378 | — | — | — |
| Premises and equipment | 1,639 | 1,598 | 1,216 | 1,274 | 1,872 | 1,696 | 1,785 | 1,870 | 1,975 | 2,057 | 1,914 |
| Goodwill | 5,040 | 4,952 | 693 | 660 | 608 | 668 | 335 | 333 | 365 | 447 | 195 |
| Other intangibles | 665 | 619 | 208 | — | — | — | — | — | — | — | — |
| Other assets | 13,490 | 13,364 | 8,490 | 7,997 | 13,975 | 8,376 | 8,717 | 5,094 | 5,020 | 4,781 | 3,226 |
| | 60,135 | 59,098 | 41,569 | 34,339 | 57,488 | 36,077 | 26,858 | 25,975 | 13,565 | 13,587 | 11,072 |
| | \$ 381,932 | \$ 362,483 | \$ 294,054 | \$ 273,298 | \$ 281,074 | \$ 247,079 | \$ 227,477 | \$ 196,482 | \$ 173,095 | \$ 164,941 | \$ 138,293 |
| Liabilities and shareholders' equity | | | | | | | | | | | |
| Deposits | | | | | | | | | | | |
| Canada | \$ 142,959 | \$ 140,558 | \$ 138,124 | \$ 129,306 | \$ 123,533 | \$ 122,721 | \$ 118,482 | \$ 114,778 | \$ 106,099 | \$ 103,755 | \$ 85,203 |
| International | 102,081 | 95,129 | 68,113 | 58,591 | 56,472 | 50,508 | 43,335 | 28,713 | 29,716 | 26,644 | 27,019 |
| | 245,040 | 235,687 | 206,237 | 187,897 | 180,005 | 173,229 | 161,817 | 143,491 | 135,815 | 130,399 | 112,222 |
| Other | | | | | | | | | | | |
| Acceptances | 8,051 | 9,923 | 11,628 | 9,257 | 10,620 | 10,561 | 7,423 | 6,300 | 6,205 | 6,302 | 5,737 |
| Securities sold short | 17,990 | 16,037 | 12,873 | 18,740 | 20,488 | 13,062 | 7,063 | 7,128 | 5,569 | 5,362 | 3,628 |
| Repurchase agreements | 21,109 | 20,864 | 9,005 | 9,396 | 11,264 | 9,458 | 16,526 | 4,090 | 5,341 | 2,533 | 787 |
| Derivative-related amounts (1) | 32,737 | 29,448 | 18,574 | 15,219 | 29,370 | 14,732 | 9,053 | 12,384 | — | — | — |
| Other liabilities | 29,821 | 23,979 | 15,912 | 15,682 | 12,883 | 10,644 | 12,135 | 10,284 | 7,986 | 8,919 | 5,232 |
| | 109,708 | 100,251 | 67,992 | 68,294 | 84,625 | 58,457 | 52,200 | 40,186 | 25,101 | 23,116 | 15,384 |
| Subordinated debentures | 6,960 | 6,861 | 5,825 | 4,596 | 4,087 | 4,227 | 3,602 | 3,528 | 3,481 | 3,410 | 3,106 |
| Non-controlling interest in subsidiaries | 1,469 | 1,479 | 703 | 103 | 499 | 531 | 108 | 107 | 93 | 86 | 75 |
| Shareholders' equity | | | | | | | | | | | |
| Capital stock | | | | | | | | | | | |
| Preferred | 1,515 | 1,990 | 2,001 | 1,973 | 2,110 | 1,757 | 1,725 | 1,962 | 2,233 | 2,215 | 1,572 |
| Common | 7,039 | 6,959 | 3,074 | 3,063 | 2,923 | 2,905 | 2,874 | 2,908 | 2,908 | 2,908 | 2,908 |
| Retained earnings | 10,473 | 9,311 | 8,314 | 7,495 | 6,803 | 5,719 | 4,825 | 4,194 | 3,476 | 2,823 | 3,041 |
| Accumulated other comprehensive income | (272) | (55) | (92) | (123) | 22 | 254 | 326 | 106 | (12) | (16) | (15) |
| | 18,755 | 18,205 | 13,297 | 12,408 | 11,858 | 10,635 | 9,750 | 9,170 | 8,605 | 7,930 | 7,506 |
| | \$ 381,932 | \$ 362,483 | \$ 294,054 | \$ 273,298 | \$ 281,074 | \$ 247,079 | \$ 227,477 | \$ 196,482 | \$ 173,095 | \$ 164,941 | \$ 138,293 |

(1) As the information is not reasonably determinable, amounts for years prior to 1995 have not been restated to reflect the presentation of derivative-related amounts on a gross basis.

Consolidated statement of income

For the year ended October 31

(C\$ millions, except per share amounts)

| | 2002 | 2001 | 2000 | 1999 | 1998 | 1997 | 1996 | 1995 | 1994 | 1993 | 1992 |
|--|-----------|-----------|-----------|-----------|-----------|----------|----------|----------|----------|----------|-----------|
| Interest income | | | | | | | | | | | |
| Loans | \$ 10,463 | \$ 12,032 | \$ 11,538 | \$ 10,386 | \$ 10,426 | \$ 9,354 | \$ 9,490 | \$ 9,820 | \$ 8,693 | \$ 8,156 | \$ 8,957 |
| Securities | 3,075 | 3,281 | 2,669 | 2,195 | 1,962 | 2,166 | 2,461 | 2,179 | 1,654 | 1,320 | 1,037 |
| Assets purchased under reverse repurchase agreements (1) | 651 | 1,163 | 1,078 | 893 | 1,169 | 568 | 366 | 237 | 206 | 91 | — |
| Deposits with banks | 482 | 831 | 824 | 726 | 750 | 983 | 891 | 792 | 454 | 296 | 396 |
| | 14,671 | 17,307 | 16,109 | 14,200 | 14,307 | 13,071 | 13,208 | 13,028 | 11,007 | 9,863 | 10,390 |
| Interest expense | | | | | | | | | | | |
| Deposits | 5,709 | 8,712 | 9,057 | 7,636 | 7,732 | 6,548 | 7,115 | 7,362 | 5,477 | 4,995 | 5,868 |
| Other liabilities | 1,405 | 1,688 | 1,429 | 1,161 | 1,172 | 1,139 | 1,126 | 792 | 761 | 567 | 322 |
| Subordinated debentures | 406 | 410 | 344 | 286 | 339 | 384 | 322 | 335 | 290 | 263 | 272 |
| | 7,520 | 10,810 | 10,830 | 9,083 | 9,243 | 8,071 | 8,563 | 8,489 | 6,528 | 5,825 | 6,462 |
| Net interest income | 7,151 | 6,497 | 5,279 | 5,117 | 5,064 | 5,000 | 4,645 | 4,539 | 4,479 | 4,038 | 3,928 |
| Provision for credit losses | 1,151 | 1,119 | 691 | 760 | 575 | 380 | 570 | 580 | 820 | 1,750 | 2,050 |
| | 6,086 | 5,378 | 4,588 | 4,357 | 4,489 | 4,620 | 4,075 | 3,959 | 3,659 | 2,288 | 1,878 |
| Non-interest revenue | | | | | | | | | | | |
| Capital market fees | 1,866 | 1,523 | 1,538 | 1,028 | 918 | 1,172 | 764 | 434 | 567 | 456 | 356 |
| Trading revenues | 1,766 | 1,820 | 1,540 | 1,106 | 752 | 606 | 368 | 362 | 345 | 414 | 387 |
| Investment management and custodial fees | 1,179 | 1,096 | 860 | 651 | 605 | 404 | 319 | 286 | 278 | 101 | 82 |
| Deposit and payment service charges | 1,041 | 887 | 756 | 688 | 664 | 690 | 701 | 681 | 661 | 649 | 654 |
| Mutual fund revenues | 723 | 692 | 624 | 556 | 537 | 354 | 241 | 190 | 202 | 64 | 37 |
| Card service revenues | 285 | 290 | 420 | 362 | 305 | 332 | 282 | 278 | 258 | 203 | 183 |
| Foreign exchange revenue, other than trading | 277 | 300 | 299 | 243 | 218 | 211 | 165 | 140 | 134 | 107 | 115 |
| Insurance revenues | 255 | 263 | 151 | 174 | 113 | 102 | 70 | 104 | 100 | 61 | 32 |
| Mortgage banking revenues | 240 | 206 | — | — | — | — | — | — | — | — | — |
| Credit fees | 223 | 237 | 212 | 189 | 183 | 169 | 153 | 156 | 156 | 152 | 152 |
| Securitization revenues | 172 | 125 | 104 | 220 | 226 | 9 | — | — | — | — | — |
| Gain (loss) on sale of securities | (95) | (128) | (11) | 28 | 343 | 37 | 107 | 17 | 49 | 169 | 14 |
| Gain from divestitures | — | 445 | — | — | — | — | — | — | — | — | — |
| Other | 647 | 399 | 187 | 246 | 133 | 202 | 96 | 90 | 113 | 75 | 90 |
| | 8,579 | 8,155 | 6,680 | 5,491 | 4,997 | 4,288 | 3,266 | 2,738 | 2,863 | 2,451 | 2,102 |
| Non-interest expense | | | | | | | | | | | |
| Human resources | 6,263 | 5,696 | 4,695 | 4,096 | 3,688 | 3,427 | 2,933 | 2,581 | 2,675 | 2,386 | 2,170 |
| Occupancy | 788 | 716 | 570 | 564 | 508 | 559 | 507 | 473 | 500 | 593 | 476 |
| Equipment | 752 | 713 | 664 | 677 | 585 | 605 | 492 | 506 | 460 | 473 | 382 |
| Communications | 790 | 679 | 695 | 699 | 665 | 587 | 523 | 461 | 450 | 377 | 372 |
| Professional fees | 419 | 411 | 267 | 274 | 286 | 228 | 165 | 147 | 113 | 86 | 88 |
| Amortization of goodwill | — | 252 | 80 | 70 | 66 | 63 | 38 | 38 | 48 | 35 | 19 |
| Amortization of other intangibles | 72 | 36 | 11 | — | — | — | — | — | — | — | — |
| Other | 1,160 | 1,138 | 646 | 761 | 712 | 602 | 509 | 469 | 415 | 465 | 410 |
| | 10,244 | 9,641 | 7,628 | 7,141 | 6,510 | 6,071 | 5,167 | 4,675 | 4,661 | 4,415 | 3,917 |
| Net income before income taxes | 4,421 | 3,892 | 3,640 | 2,707 | 2,976 | 2,837 | 2,174 | 2,022 | 1,861 | 324 | 63 |
| Income taxes | 1,415 | 1,350 | 1,412 | 974 | 1,128 | 1,106 | 795 | 741 | 655 | (5) | (65) |
| Net income before non-controlling interest | 3,006 | 2,542 | 2,228 | 1,733 | 1,848 | 1,731 | 1,379 | 1,281 | 1,206 | 329 | 128 |
| Non-controlling interest | 108 | 107 | 20 | 8 | 76 | 77 | 49 | 23 | 37 | 29 | 21 |
| Net income | \$ 2,898 | \$ 2,435 | \$ 2,208 | \$ 1,725 | \$ 1,772 | \$ 1,654 | \$ 1,330 | \$ 1,258 | \$ 1,169 | \$ 300 | \$ 107 |
| Preferred share dividends | 98 | 135 | 134 | 157 | 145 | 131 | 144 | 164 | 168 | 154 | 123 |
| Net income available to common shareholders | \$ 2,800 | \$ 2,300 | \$ 2,074 | \$ 1,568 | \$ 1,627 | \$ 1,523 | \$ 1,186 | \$ 1,094 | \$ 1,001 | \$ 146 | \$ (16) |
| Earnings per share (loss) | | | | | | | | | | | |
| Basic | \$ 4.16 | \$ 3.58 | \$ 3.42 | \$ 2.50 | \$ 2.64 | \$ 2.46 | \$ 1.89 | \$ 1.74 | \$ 1.59 | \$ 0.23 | \$ (0.03) |
| Diluted | 4.12 | 3.55 | 3.40 | 2.48 | 2.58 | 2.42 | 1.89 | 1.74 | 1.59 | 0.23 | (0.03) |

(1) Amounts for assets purchased under reverse repurchase agreements are included in loans for 1992.

Consolidated statement of changes in shareholders' equity

| For the year ended October 31 (C\$ millions) | 2002 | 2001 | 2000 | 1999 | 1998 | 1997 | 1996 | 1995 | 1994 | 1993 | 1992 |
|---|------------------|------------------|------------------|------------------|------------------|------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Preferred shares | | | | | | | | | | | |
| Balance at beginning of year | \$ 1,990 | \$ 2,001 | \$ 1,973 | \$ 2,110 | \$ 1,757 | \$ 1,725 | \$ 1,962 | \$ 2,233 | \$ 2,215 | \$ 1,572 | \$ 1,636 |
| Issued | — | 250 | — | 296 | 300 | — | — | — | — | 612 | — |
| Redeemed for cancellation | (464) | (295) | — | (393) | — | — | (236) | (267) | — | — | (99) |
| Issuance costs, net of related income taxes | — | (3) | — | (9) | (7) | — | — | — | — | (11) | — |
| Transition adjustment | (11) | 37 | 28 | (31) | 60 | 32 | (1) | (4) | 18 | 42 | 35 |
| Balance at end of year | 1,515 | 1,990 | 2,001 | 1,973 | 2,110 | 1,757 | 1,725 | 1,962 | 2,233 | 2,215 | 1,572 |
| Common shares | | | | | | | | | | | |
| Balance at beginning of year | 6,959 | 3,074 | 3,063 | 2,923 | 2,905 | 2,874 | 2,908 | 2,908 | 2,908 | 2,908 | 2,724 |
| Issued | 233 | 4,009 | 109 | 192 | 18 | 69 | — | — | — | — | 184 |
| Issuance costs, net of related income taxes | (1) | (12) | — | — | — | — | — | — | — | — | — |
| Purchased for cancellation | (152) | (112) | (98) | (52) | — | (38) | (34) | — | — | — | — |
| Balance at end of year | 7,039 | 6,959 | 3,074 | 3,063 | 2,923 | 2,905 | 2,874 | 2,908 | 2,908 | 2,908 | 2,908 |
| Retained earnings | | | | | | | | | | | |
| Balance at beginning of year (1) | 9,311 | 8,314 | 7,495 | 6,803 | 5,719 | 4,825 | 4,194 | 3,476 | 2,839 | 3,041 | 3,421 |
| Net income | 2,898 | 2,435 | 2,208 | 1,725 | 1,772 | 1,654 | 1,330 | 1,258 | 1,169 | 300 | 107 |
| Dividends – preferred | (98) | (135) | (134) | (157) | (145) | (131) | (144) | (164) | (168) | (154) | (123) |
| Dividends – common | (1,022) | (897) | (689) | (588) | (543) | (469) | (418) | (371) | (364) | (364) | (361) |
| Premium paid on common shares purchased | (612) | (397) | (562) | (281) | — | (160) | (136) | — | — | — | — |
| Issuance costs, net of related income taxes | (4) | (9) | (4) | (7) | — | — | (1) | (5) | — | — | (3) |
| Balance at end of year | 10,473 | 9,311 | 8,314 | 7,495 | 6,803 | 5,719 | 4,825 | 4,194 | 3,476 | 2,823 | 3,041 |
| Accumulated other comprehensive income (loss), net of related income taxes | | | | | | | | | | | |
| Unrealized gains and losses on available for sale securities (2) | 202 | 190 | (56) | (85) | 56 | 283 | 349 | 126 | — | — | — |
| Unrealized foreign currency translation gains and losses, net of hedging activities | (54) | (38) | (36) | (38) | (34) | (29) | (23) | (20) | (12) | (16) | (15) |
| Gains and losses on derivatives designated as cash flow hedges | (127) | (190) | — | — | — | — | — | — | — | — | — |
| Additional pension obligation | (293) | (17) | — | — | — | — | — | — | — | — | — |
| | (272) | (55) | (92) | (123) | 22 | 254 | 326 | 106 | (12) | (16) | (15) |
| Shareholders' equity at end of year | \$ 18,755 | \$ 18,205 | \$ 13,297 | \$ 12,408 | \$ 11,858 | \$ 10,635 | \$ 9,750 | \$ 9,170 | \$ 8,605 | \$ 7,930 | \$ 7,506 |
| Comprehensive income, net of related income taxes | | | | | | | | | | | |
| Net income | \$ 2,898 | \$ 2,435 | \$ 2,208 | \$ 1,725 | \$ 1,772 | \$ 1,654 | \$ 1,330 | \$ 1,258 | \$ 1,169 | \$ 300 | \$ 107 |
| Other comprehensive income | | | | | | | | | | | |
| Change in unrealized gains and losses on available for sale securities (2) | 12 | 246 | 29 | (141) | (227) | (66) | 223 | 126 | — | — | — |
| Change in unrealized foreign currency translation gains and losses | (59) | 473 | (2) | (205) | 164 | 129 | (12) | (23) | 96 | (4) | 16 |
| Impact of hedging unrealized foreign currency translation gains and losses | 43 | (475) | 4 | 201 | (169) | (135) | 9 | 15 | (92) | 3 | (12) |
| Cumulative effect of initial adoption of FAS 133 | — | 60 | — | — | — | — | — | — | — | — | — |
| Change in gains and losses on derivatives designated as cash flow hedges | (50) | (250) | — | — | — | — | — | — | — | — | — |
| Reclassification to earnings of gains and losses on cash flow hedges | 113 | — | — | — | — | — | — | — | — | — | — |
| Additional pension obligation | (276) | (17) | — | — | — | — | — | — | — | — | — |
| Total comprehensive income | \$ 2,681 | \$ 2,472 | \$ 2,239 | \$ 1,580 | \$ 1,540 | \$ 1,582 | \$ 1,550 | \$ 1,376 | \$ 1,173 | \$ 299 | \$ 111 |

(1) Retained earnings at the beginning of 1994 was increased by \$16 million as a result of the adoption of FAS 109, *Accounting for Income Taxes*.(2) Effective 1995, the bank adopted FAS 115, *Accounting for Certain Investments in Debt and Equity Securities*.

Risk profile

| As at October 31 (C\$ millions, except percentage amounts) | | 2002 | 2001 | 2000 | 1999 | 1998 | 1997 | 1996 | 1995 | 1994 | 1993 | 1992 | | | | | | | | | | |
|--|----|---------|------|---------|------|-------|------|---------|------|-------|------|-------|----|-------|----|---------|----|---------|----|---------|----|-------|
| Nonaccrual loans | | | | | | | | | | | | | | | | | | | | | | |
| Beginning of year | \$ | 2,465 | \$ | 1,678 | \$ | 1,704 | \$ | 2,001 | \$ | 1,819 | \$ | 2,376 | \$ | 2,944 | \$ | 4,424 | \$ | 7,582 | \$ | 7,056 | \$ | 3,924 |
| Net additions (reductions) | | 1,280 | | 1,912 | | 813 | | 743 | | 628 | | 81 | | 384 | | (255) | | (1,128) | | 1,643 | | 3,639 |
| Charge-offs and adjustments | | (1,457) | | (1,125) | | (839) | | (1,040) | | (446) | | (638) | | (952) | | (1,225) | | (2,030) | | (1,117) | | (507) |
| End of year | \$ | 2,288 | \$ | 2,465 | \$ | 1,678 | \$ | 1,704 | \$ | 2,001 | \$ | 1,819 | \$ | 2,376 | \$ | 2,944 | \$ | 4,424 | \$ | 7,582 | \$ | 7,056 |
| As a % of loans and acceptances | | 1.3% | | 1.4% | | 1.0% | | 1.1% | | 1.3% | | 1.2% | | 1.8% | | 2.4% | | 3.7% | | 6.2% | | 6.5% |
| Allowance for credit losses | | | | | | | | | | | | | | | | | | | | | | |
| Allocated specific | \$ | 894 | \$ | 951 | \$ | 747 | \$ | 786 | \$ | 1,176 | \$ | 932 | \$ | 1,091 | \$ | 1,439 | \$ | 1,962 | \$ | 2,667 | \$ | 1,867 |
| Allocated country risk | | — | | 31 | | 28 | | 34 | | 40 | | 436 | | 444 | | 930 | | 940 | | 1,107 | | 1,383 |
| Allocated general (1) | | 1,169 | | 1,185 | | 863 | | 790 | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. |
| Total allocated (1) | | 2,063 | | 2,167 | | 1,638 | | 1,610 | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. |
| Unallocated (1) | | 251 | | 225 | | 337 | | 290 | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. |
| Total | \$ | 2,314 | \$ | 2,392 | \$ | 1,975 | \$ | 1,900 | \$ | 2,066 | \$ | 2,118 | \$ | 2,235 | \$ | 2,669 | \$ | 3,202 | \$ | 4,324 | \$ | 3,575 |
| Composition of allowance | | | | | | | | | | | | | | | | | | | | | | |
| Allowance for loan losses | \$ | 2,203 | \$ | 2,278 | \$ | 1,871 | \$ | 1,884 | \$ | 2,026 | \$ | 1,769 | \$ | 1,875 | \$ | 2,003 | \$ | 2,559 | \$ | 4,255 | \$ | 3,575 |
| Allowance for off-balance sheet and other items (2) | | 109 | | 109 | | 98 | | — | | — | | — | | — | | — | | — | | — | | — |
| Allowance for tax-exempt securities | | 2 | | 5 | | 6 | | 16 | | 40 | | 30 | | 34 | | — | | — | | — | | — |
| Allowance for country risk securities | | — | | — | | — | | — | | — | | 319 | | 326 | | 666 | | 643 | | 69 | | — |
| Total | \$ | 2,314 | \$ | 2,392 | \$ | 1,975 | \$ | 1,900 | \$ | 2,066 | \$ | 2,118 | \$ | 2,235 | \$ | 2,669 | \$ | 3,202 | \$ | 4,324 | \$ | 3,575 |
| Allowance for loan losses as a % of loans and acceptances | | 1.2% | | 1.3% | | 1.1% | | 1.2% | | 1.3% | | 1.2% | | 1.4% | | 1.6% | | 2.2% | | 3.5% | | 3.3% |
| Allowance for loan losses as a % of loans, acceptances and reverse repurchase agreements | | 1.0 | | 1.0 | | 1.0 | | 1.1 | | 1.1 | | 1.1 | | 1.3 | | 1.6 | | 2.1 | | 3.4 | | 3.3 |
| Allowance for loan losses as a % of nonaccrual loans, excluding LDCs | | 96 | | 93 | | 112 | | 112 | | 103 | | 94 | | 77 | | 60 | | 52 | | 52 | | 41 |
| Provision for credit losses | | | | | | | | | | | | | | | | | | | | | | |
| Allocated specific | \$ | 1,065 | \$ | 1,049 | \$ | 571 | \$ | 530 | \$ | 555 | \$ | 330 | \$ | 470 | \$ | 580 | \$ | 1,070 | \$ | 1,775 | \$ | 2,025 |
| Allocated country risk | | — | | — | | — | | — | | (80) | | — | | (300) | | — | | — | | (250) | | (300) |
| Allocated general (3) | | (22) | | 205 | | 73 | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. |
| Total allocated (3) | | 1,043 | | 1,254 | | 644 | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. |
| Unallocated (3) | | 22 | | (135) | | 47 | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. | | n.a. |
| Total | \$ | 1,065 | \$ | 1,119 | \$ | 691 | \$ | 760 | \$ | 575 | \$ | 380 | \$ | 570 | \$ | 580 | \$ | 820 | \$ | 1,750 | \$ | 2,050 |
| Allocated specific provisions as a % of average loans and acceptances | | .60% | | .61% | | .36% | | .34% | | .36% | | .23% | | .37% | | .48% | | .88% | | 1.64% | | 1.90% |
| Allocated specific provisions as a % of average loans, acceptances and reverse repurchase agreements | | .50 | | .52 | | .31 | | .30 | | .31 | | .21 | | .36 | | .46 | | .84 | | 1.60 | | 1.90 |
| Provision as a % of average loans and acceptances | | .60 | | .65 | | .43 | | .49 | | .37 | | .27 | | .45 | | .48 | | .67 | | 1.61 | | 1.93 |
| Provision as a % of average loans, acceptances and reverse repurchase agreements | | .50 | | .55 | | .38 | | .43 | | .32 | | .24 | | .43 | | .46 | | .65 | | 1.58 | | 1.93 |
| Net charge-offs | \$ | 1,259 | \$ | 940 | \$ | 677 | \$ | 958 | \$ | 692 | \$ | 528 | \$ | 1,001 | \$ | 1,105 | \$ | 1,979 | \$ | 1,187 | \$ | 547 |
| As a % of average loans and acceptances | | .71% | | .55% | | .42% | | .62% | | .45% | | .37% | | .79% | | .91% | | 1.63% | | 1.09% | | .51% |

(1) The allocated general and the unallocated amounts totalled \$850 million in 1998, \$750 million in 1997, \$700 million in 1996, \$300 million in 1995, \$300 million in 1994, \$550 million in 1993 and \$325 million in 1992. These were not separated into the allocated general and unallocated components. The amounts prior to 1999 do not include the allocated general allowance.

(2) During 2000, the allowance for off-balance sheet and other items has been separated and reported under other liabilities. Previously, the amount was included in the allowance for loan losses.

(3) The allocated general provision and the unallocated provision totalled \$230 million in 1999, \$100 million in 1998, \$50 million in 1997, \$400 million in 1996, nil in 1995, \$(250) million in 1994, \$225 million in 1993 and \$325 million in 1992. These were not separated into the allocated general and unallocated components.

Financial highlights

(C\$ millions, taxable equivalent basis, except per share and percentage amounts)

| | 2002 | 2001 | 2000 | 1999 | 1998 | 1997 | 1996 | 1995 | 1994 | 1993 | 1992 |
|---|-------------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|
| Performance ratios | | | | | | | | | | | |
| Return on common equity | 16.6% | 16.6% | 19.3% | 15.3% | 17.6% | 18.3% | 15.7% | 16.2% | 16.8% | 2.4% | (.3)% |
| Cash return on common equity (1) | 17.0 | 18.6 | 20.2 | 15.9 | 18.3 | 19.1 | 16.2 | 16.8 | 17.6 | 3.0 | – |
| Return on assets | .78 | .73 | .78 | .64 | .68 | .69 | .65 | .68 | .70 | .21 | .08 |
| Return on assets after preferred dividends | .75 | .69 | .73 | .58 | .62 | .64 | .58 | .59 | .60 | .10 | (.01) |
| Net interest margin (2) | 1.93 | 1.97 | 1.87 | 1.91 | 1.95 | 2.10 | 2.28 | 2.49 | 2.72 | 2.88 | 2.93 |
| Non-interest revenue as a % of gross revenues | 54.4 | 55.5 | 55.7 | 51.6 | 49.5 | 46.0 | 41.1 | 37.4 | 38.7 | 37.4 | 34.5 |
| Average balances and year-end off-balance sheet data | | | | | | | | | | | |
| Averages | | | | | | | | | | | |
| Assets (3) | \$ 371,700 | \$ 331,600 | \$ 284,100 | \$ 270,000 | \$ 261,500 | \$ 239,800 | \$ 205,200 | \$ 183,900 | \$ 166,700 | \$ 142,500 | \$ 136,200 |
| Loans and acceptances | 177,464 | 172,136 | 159,957 | 155,635 | 154,954 | 142,349 | 126,849 | 121,069 | 121,741 | 108,562 | 106,376 |
| Deposits | 242,269 | 221,419 | 196,066 | 184,796 | 178,688 | 166,249 | 147,391 | 136,686 | 133,550 | 114,835 | 108,609 |
| Common equity | 16,880 | 13,899 | 10,725 | 10,268 | 9,255 | 8,303 | 7,543 | 6,749 | 5,964 | 6,052 | 6,313 |
| Total equity | 18,562 | 15,935 | 12,703 | 12,481 | 11,227 | 10,044 | 9,488 | 8,942 | 8,233 | 8,116 | 7,938 |
| Assets under administration (4) | 1,365,900 | 1,342,500 | 1,175,200 | 967,800 | 829,200 | 783,300 | 522,100 | 407,700 | 346,800 | 274,300 | |
| Assets under management (4) | 90,800 | 100,000 | 92,300 | 81,600 | 73,400 | 67,700 | 51,200 | 40,400 | 39,100 | 33,100 | |
| Capital ratios (Cdn) (5) | | | | | | | | | | | |
| Tier 1 capital | \$ 15,380 | \$ 14,851 | \$ 13,567 | \$ 12,026 | \$ 11,593 | \$ 10,073 | \$ 9,037 | \$ 8,421 | \$ 7,660 | \$ 6,910 | \$ 6,740 |
| Total capital | 21,012 | 20,171 | 19,044 | 16,698 | 16,480 | 14,705 | 12,069 | 11,913 | 11,525 | 10,941 | 10,483 |
| Total risk-adjusted assets | 165,559 | 171,047 | 158,364 | 149,078 | 157,064 | 147,672 | 128,163 | 121,350 | 120,158 | 117,043 | 114,298 |
| Common equity to risk-adjusted assets | 10.4% | 9.4% | 7.3% | 7.1% | 6.2% | 5.8% | 6.0% | 5.8% | 5.3% | 4.9% | 5.2% |
| Tier 1 capital ratio | 9.3 | 8.7 | 8.6 | 8.1 | 7.4 | 6.8 | 7.0 | 6.9 | 6.4 | 5.9 | 5.9 |
| Total capital ratio | 12.7 | 11.8 | 12.0 | 11.2 | 10.5 | 10.0 | 9.4 | 9.8 | 9.6 | 9.3 | 9.2 |
| Capital ratios (U.S.) (6) | | | | | | | | | | | |
| Tier 1 capital | \$ 13,992 | \$ 13,817 | \$ 12,409 | \$ 11,334 | \$ 10,796 | \$ 9,556 | \$ 8,740 | \$ 8,612 | \$ 7,660 | \$ 6,910 | \$ 6,740 |
| Total capital | 19,624 | 19,137 | 17,898 | 15,991 | 15,990 | 14,666 | 12,245 | 12,399 | 11,525 | 10,941 | 10,483 |
| Total risk-adjusted assets | 164,930 | 171,188 | 158,594 | 149,537 | 157,720 | 149,392 | 128,804 | 120,593 | 120,158 | 117,043 | 114,298 |
| Common equity to risk-adjusted assets | 10.5% | 9.5% | 7.2% | 7.0% | 6.1% | 5.8% | 6.0% | 5.9% | 5.3% | 4.9% | 5.2% |
| Tier 1 capital ratio | 8.5 | 8.1 | 7.8 | 7.6 | 6.8 | 6.4 | 6.8 | 7.1 | 6.4 | 5.9 | 5.9 |
| Total capital ratio | 11.9 | 11.2 | 11.3 | 10.7 | 10.1 | 9.8 | 9.5 | 10.3 | 9.6 | 9.3 | 9.2 |
| Common share information | | | | | | | | | | | |
| Shares outstanding (in thousands) | | | | | | | | | | | |
| End of year | 665,257 | 674,021 | 602,398 | 617,768 | 617,581 | 616,671 | 621,059 | 628,310 | 628,310 | 628,310 | 628,310 |
| Average basic | 672,571 | 641,516 | 606,389 | 626,158 | 617,324 | 617,812 | 628,242 | 628,310 | 628,310 | 628,310 | 621,086 |
| Average diluted | 679,153 | 647,216 | 609,865 | 632,305 | 633,626 | 632,052 | 628,242 | 628,310 | 628,310 | 628,310 | 621,086 |
| Dividends per share | \$ 1.52 | \$ 1.38 | \$ 1.14 | \$ 0.94 | \$ 0.88 | \$ 0.76 | \$ 0.67 | \$ 0.59 | \$ 0.58 | \$ 0.58 | \$ 0.58 |
| Book value per share | 25.91 | 24.06 | 18.75 | 16.89 | 15.81 | 14.29 | 12.77 | 11.47 | 10.14 | 9.10 | 9.44 |
| Share price – High (7) | 58.89 | 53.25 | 48.88 | 42.13 | 46.10 | 38.23 | 22.20 | 15.69 | 15.94 | 14.44 | 14.50 |
| Share price – Low (7) | 45.05 | 41.60 | 27.25 | 29.65 | 28.75 | 22.00 | 14.88 | 12.94 | 12.57 | 11.00 | 10.75 |
| Close | 54.41 | 46.80 | 48.30 | 31.73 | 35.55 | 37.68 | 22.15 | 15.07 | 14.19 | 13.63 | 12.07 |
| Price/earnings multiple (8) | 12.6 | 13.4 | 11.2 | 14.5 | 14.5 | 12.4 | 9.8 | 8.2 | 9.0 | – | – |
| Dividend yield (9) | 2.9% | 2.9% | 3.0% | 2.6% | 2.4% | 2.5% | 3.6% | 4.1% | 4.1% | 4.6% | 4.6% |
| Dividend payout ratio (10) | 37 | 39 | 33 | 37 | 33 | 31 | 35 | 34 | 36 | – | – |
| Number of: | | | | | | | | | | | |
| Employees (11) | 59,549 | 57,568 | 49,232 | 51,891 | 51,776 | 48,816 | 46,205 | 49,011 | 49,208 | 52,745 | 49,628 |
| Automated banking machines | 4,486 | 4,548 | 4,517 | 4,585 | 4,317 | 4,248 | 4,215 | 4,079 | 3,948 | 3,981 | 3,828 |
| Service delivery units | | | | | | | | | | | |
| Canada | 1,311 | 1,317 | 1,333 | 1,410 | 1,422 | 1,453 | 1,493 | 1,577 | 1,596 | 1,731 | 1,661 |
| International (12) | 807 | 724 | 306 | 99 | 106 | 105 | 103 | 105 | 97 | 95 | 83 |

(1) Cash return on common equity is computed by adding back to net income the after-tax amount of amortization of goodwill and other intangibles.

(2) Net interest income as a percentage of average assets.

(3) As the information is not reasonably determinable, amounts for years prior to 1995 have not been restated to reflect the presentation of derivative-related amounts on a gross basis.

(4) Amounts prior to 1996 are as at September 30. Assets under administration and assets under management balances were not reported prior to 1993.

(5) Using guidelines issued by the Superintendent of Financial Institutions Canada and Canadian GAAP financial information.

(6) Using guidelines issued by the Board of Governors of the Federal Reserve System in the United States and U.S. GAAP financial information.

(7) Intraday high and low share prices.

(8) Average of high and low common share price divided by diluted earnings per share. The multiples for 1993 and 1992 are not meaningful.

(9) Dividends per common share divided by the average of high and low share price.

(10) Common dividends as a percentage of net income after preferred dividends. The ratios for 1993 and 1992 are not meaningful.

(11) On a full-time equivalent basis.

(12) International service delivery units include branches, specialized business centres, representative offices and agencies.

Quarterly highlights

| (C\$ millions, taxable equivalent basis, except per share and percentage amounts) | 2002 | | | | 2001 | | | |
|---|------------|------------|------------|------------|------------|------------|------------|------------|
| | Q4 | Q3 | Q2 | Q1 | Q4 | Q3 | Q2 | Q1 |
| Consolidated statement of income | | | | | | | | |
| Net interest income | \$ 1,818 | \$ 1,770 | \$ 1,732 | \$ 1,871 | \$ 1,772 | \$ 1,715 | \$ 1,569 | \$ 1,473 |
| Provision for credit losses | (235) | (216) | (328) | (286) | (425) | (236) | (210) | (248) |
| Non-interest revenue | 2,103 | 2,101 | 2,189 | 2,186 | 2,265 | 1,963 | 1,940 | 1,987 |
| Non-interest expense | (2,601) | (2,515) | (2,519) | (2,609) | (2,636) | (2,598) | (2,263) | (2,144) |
| Income taxes | (325) | (391) | (338) | (401) | (268) | (380) | (383) | (351) |
| Non-controlling interest | (28) | (27) | (26) | (27) | (28) | (28) | (29) | (22) |
| Net income | \$ 732 | \$ 722 | \$ 710 | \$ 734 | \$ 680 | \$ 436 | \$ 624 | \$ 695 |
| Cash net income (1) | \$ 749 | \$ 738 | \$ 724 | \$ 751 | \$ 803 | \$ 518 | \$ 674 | \$ 726 |
| Core cash net income (1) | \$ 749 | \$ 738 | \$ 724 | \$ 751 | \$ 564 | \$ 664 | \$ 674 | \$ 615 |
| Earnings per share (2) | | | | | | | | |
| Basic | \$ 1.06 | \$ 1.04 | \$ 1.02 | \$ 1.05 | \$.95 | \$.60 | \$.96 | \$ 1.09 |
| Diluted | 1.05 | 1.02 | 1.01 | 1.04 | .94 | .60 | .95 | 1.08 |
| Cash diluted (1) | 1.07 | 1.05 | 1.03 | 1.07 | 1.12 | .72 | 1.03 | 1.13 |
| Core cash diluted (1) | 1.07 | 1.05 | 1.03 | 1.07 | .78 | .94 | 1.03 | .96 |
| Performance ratios | | | | | | | | |
| Return on common equity | 16.3% | 16.1% | 16.8% | 17.1% | 15.7% | 10.8% | 19.2% | 21.9% |
| Cash return on common equity (1) | 16.7 | 16.5 | 17.1 | 17.5 | 18.6 | 13.1 | 20.8 | 23.0 |
| Core cash return on common equity (1) | 16.7 | 16.5 | 17.1 | 17.5 | 12.9 | 17.0 | 20.8 | 19.3 |
| Return on assets | .76 | .78 | .78 | .79 | .78 | .50 | .78 | .89 |
| Return on assets after preferred dividends | .73 | .75 | .76 | .77 | .74 | .46 | .74 | .85 |
| Net interest margin (3) | 1.89 | 1.91 | 1.91 | 2.03 | 2.03 | 1.98 | 1.97 | 1.89 |
| Non-interest revenue as a % of gross revenues | 53.6 | 54.3 | 55.8 | 53.9 | 56.1 | 53.4 | 55.3 | 57.4 |
| Consolidated balance sheet | | | | | | | | |
| Assets | | | | | | | | |
| Cash resources and securities | \$ 116,646 | \$ 111,203 | \$ 110,105 | \$ 103,920 | \$ 98,616 | \$ 95,684 | \$ 87,408 | \$ 83,634 |
| Assets purchased under reverse repurchase agreements | 35,831 | 34,938 | 33,373 | 30,503 | 35,870 | 25,101 | 26,453 | 21,713 |
| Residential mortgage loans | 72,842 | 70,641 | 70,118 | 69,438 | 67,444 | 66,499 | 64,559 | 63,418 |
| Personal loans | 31,956 | 32,222 | 32,292 | 31,600 | 32,511 | 32,264 | 29,713 | 30,573 |
| Credit card loans | 4,914 | 4,774 | 4,445 | 4,338 | 4,283 | 4,128 | 4,862 | 4,961 |
| Business and government loans | 61,811 | 64,187 | 63,602 | 64,285 | 66,939 | 65,111 | 59,989 | 60,328 |
| Allowance for loan losses | (2,203) | (2,218) | (2,338) | (2,345) | (2,278) | (2,173) | (1,951) | (1,947) |
| Other assets | 60,135 | 61,789 | 49,650 | 56,661 | 59,098 | 48,288 | 47,910 | 44,131 |
| | \$ 381,932 | \$ 377,536 | \$ 361,247 | \$ 358,400 | \$ 362,483 | \$ 334,902 | \$ 318,943 | \$ 306,811 |
| Liabilities and shareholders' equity | | | | | | | | |
| Deposits – Canada | \$ 142,959 | \$ 138,801 | \$ 139,125 | \$ 139,862 | \$ 140,558 | \$ 138,095 | \$ 141,000 | \$ 135,093 |
| Deposits – International | 102,081 | 107,239 | 98,626 | 96,410 | 95,129 | 87,226 | 73,506 | 71,213 |
| Other liabilities | 109,708 | 103,791 | 96,181 | 95,035 | 100,251 | 82,917 | 81,117 | 78,133 |
| Subordinated debentures | 6,960 | 7,318 | 7,245 | 7,340 | 6,861 | 6,649 | 6,992 | 6,447 |
| Non-controlling interest in subsidiaries | 1,469 | 1,444 | 1,466 | 1,440 | 1,479 | 1,453 | 1,481 | 1,453 |
| Total equity | 18,755 | 18,943 | 18,604 | 18,313 | 18,205 | 18,562 | 14,847 | 14,472 |
| | \$ 381,932 | \$ 377,536 | \$ 361,247 | \$ 358,400 | \$ 362,483 | \$ 334,902 | \$ 318,943 | \$ 306,811 |
| Selected average balances and off-balance sheet data | | | | | | | | |
| Averages | | | | | | | | |
| Assets | \$ 382,200 | \$ 367,400 | \$ 371,100 | \$ 366,400 | \$ 346,300 | \$ 344,100 | \$ 326,900 | \$ 309,000 |
| Loans and acceptances | 178,004 | 175,364 | 177,438 | 179,128 | 178,042 | 173,951 | 168,600 | 167,863 |
| Deposits | 248,828 | 238,647 | 239,470 | 242,013 | 232,928 | 224,268 | 215,988 | 210,238 |
| Common equity | 17,223 | 17,139 | 16,770 | 16,459 | 16,450 | 14,596 | 12,639 | 11,955 |
| Total equity | 18,855 | 18,800 | 18,445 | 18,210 | 18,497 | 16,725 | 14,648 | 13,952 |
| Assets under administration | 1,365,900 | 1,413,100 | 1,442,800 | 1,426,600 | 1,342,500 | 1,271,800 | 1,198,700 | 1,242,800 |
| Assets under management | 90,800 | 94,200 | 96,200 | 103,300 | 100,000 | 110,500 | 110,400 | 112,500 |
| Provision for credit losses | | | | | | | | |
| Allocated specific | \$ 235 | \$ 216 | \$ 328 | \$ 286 | \$ 425 | \$ 236 | \$ 210 | \$ 178 |
| Allocated general | (15) | 4 | – | (11) | 108 | – | – | 97 |
| Total allocated | 220 | 220 | 328 | 275 | 533 | 236 | 210 | 275 |
| Unallocated | 15 | (4) | – | 11 | (108) | – | – | (27) |
| Total | \$ 235 | \$ 216 | \$ 328 | \$ 286 | \$ 425 | \$ 236 | \$ 210 | \$ 248 |
| Nonaccrual loans as a % of loans and acceptances | | | | | | | | |
| | 1.27% | 1.32% | 1.41% | 1.52% | 1.36% | 1.23% | 1.18% | 1.03% |
| Capital ratios (Canadian basis) | | | | | | | | |
| Common equity/risk-adjusted assets | 10.4% | 10.2% | 10.0% | 9.8% | 9.4% | 9.5% | 8.0% | 7.6% |
| Tier 1 | 9.3 | 9.1 | 9.0 | 8.8 | 8.7 | 9.3 | 8.8 | 8.3 |
| Total | 12.7 | 12.7 | 12.6 | 12.3 | 11.8 | 12.3 | 12.3 | 11.5 |
| Capital ratios (U.S. basis) | | | | | | | | |
| Common equity/risk-adjusted assets | 10.5% | 10.3% | 10.0% | 9.8% | 9.5% | 9.5% | 8.1% | 7.7% |
| Tier 1 | 8.5 | 8.5 | 8.4 | 8.1 | 8.1 | 8.5 | 8.4 | 8.0 |
| Total | 11.9 | 12.0 | 11.9 | 11.6 | 11.2 | 11.6 | 11.9 | 11.1 |
| Common share information | | | | | | | | |
| Shares outstanding (in thousands) | | | | | | | | |
| End of period | 665,257 | 671,671 | 673,860 | 673,596 | 674,021 | 683,312 | 616,516 | 616,209 |
| Average basic | 668,868 | 673,787 | 673,751 | 674,465 | 681,758 | 658,296 | 616,365 | 608,824 |
| Average diluted | 676,010 | 680,712 | 680,336 | 679,729 | 687,334 | 663,996 | 621,907 | 614,686 |
| Dividends per share | \$.40 | \$.38 | \$.38 | \$.36 | \$.36 | \$.36 | \$.33 | \$.33 |
| Book value per share | 25.91 | 25.71 | 25.13 | 24.70 | 24.06 | 23.87 | 20.82 | 20.26 |
| Common share price – High (4) | 57.55 | 58.89 | 57.07 | 52.45 | 53.25 | 51.50 | 51.25 | 52.80 |
| Low (4) | 48.80 | 45.05 | 46.36 | 46.81 | 41.60 | 42.80 | 42.42 | 45.10 |
| Close | 54.41 | 53.45 | 54.97 | 50.00 | 46.80 | 50.96 | 42.95 | 48.20 |
| Dividend yield | 3.0% | 2.9% | 2.9% | 2.9% | 3.0% | 3.1% | 2.8% | 2.7% |
| Dividend payout ratio | 38% | 37% | 37% | 34% | 38% | 62% | 35% | 31% |

- Cash net income, cash diluted earnings per share and cash return on common equity are computed by adding back to net income the after-tax amount of amortization of goodwill and other intangibles. Further deducting the impact of special items results in core cash net income, core cash diluted earnings per share and core cash return on common equity.
- Earnings per share for the year may not equal the sum of the quarters.
- Net interest income as a percentage of average assets.
- Intraday high and low share prices.

Financial review

Canadian GAAP

Caution regarding forward-looking statements

From time to time, we make written and oral forward-looking statements, included in this Annual Report, in other filings with Canadian regulators or the U.S. Securities and Exchange Commission, in reports to shareholders and in other communications, which are made pursuant to the "safe harbor" provisions of the United States *Private Securities Litigation Reform Act of 1995*. These forward-looking statements include, among others, statements with respect to our objectives for 2003, and the medium and long terms, and strategies to achieve those objectives, as well as statements with respect to our beliefs, plans, expectations, anticipations, estimates and intentions. The words "may," "could," "should," "would," "suspect," "outlook," "believe," "anticipate," "estimate," "expect," "intend," "plan," and words and expressions of similar import are intended to identify forward-looking statements.

By their very nature, forward-looking statements involve inherent risks and uncertainties, both general and specific, and risks exist that predictions, forecasts, projections and other forward-looking statements will not be achieved. We caution readers not to place undue reliance on these statements as a number of important factors could cause actual results to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements. These factors include, but are not limited to, the strength of the Canadian economy in general and the strength of the local economies within Canada in which we conduct operations; the strength of the United States economy and

the economies of other nations in which we conduct significant operations; the effects of changes in monetary and fiscal policy, including changes in interest rate policies of the Bank of Canada and the Board of Governors of the Federal Reserve System in the United States; changes in trade policy; the effects of competition in the markets in which we operate; inflation; capital market and currency market fluctuations; the timely development and introduction of new products and services in receptive markets; the impact of changes in the laws and regulations regulating financial services (including banking, insurance and securities); changes in tax laws; technological changes; our ability to complete strategic acquisitions and to integrate acquisitions; unexpected judicial or regulatory proceedings; unexpected changes in consumer spending and saving habits; the possible impact on our businesses of international conflicts and other developments including those relating to the war on terrorism; and our anticipation of and success in managing the risks implicated by the foregoing.

We caution that the foregoing list of important factors is not exhaustive. When relying on our forward-looking statements to make decisions, investors and others should carefully consider the foregoing factors and other uncertainties and potential events. We do not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on our behalf.

Management's discussion and analysis

We evaluate our performance on a reported basis (i.e., as reported in our consolidated financial statements prepared in accordance with Canadian generally accepted accounting principles (GAAP)) as well as on a core basis (i.e., excluding special items). We view special items as transactions that are not part of normal day-to-day business operations or are unusual in nature, thereby obscuring or distorting our analysis of trends. The special items in 2001, shown in Table 6 on page 27A, total \$230 million and include gains on dispositions, a U.S. retail banking restructuring charge, income tax related to these items, and a tax expense resulting from enactments of tax rate reductions. There were no special items in 2002. Certain earnings measures, such as core earnings, do not have a standardized meaning prescribed by GAAP and therefore are unlikely to be comparable to similar measures presented by other companies. Our recent U.S. acquisitions include RBC Centura Banks, Inc. (now

includes Eagle Bancshares, Inc., RBC Mortgage and what was previously Security First Network Bank (SFNB)), RBC Liberty Insurance and RBC Dain Rauscher (includes Tucker Anthony Sutro Corporation). We present information on a core basis because some investors may also find it useful in evaluating financial performance and analyzing trends in our businesses.

The analysis and discussion that follows on pages 22A to 66A contains comparisons to 2001 that are generally based on the 2001 core numbers (i.e., excluding special items shown on page 27A). The consolidated financial statements prepared in accordance with Canadian GAAP are on pages 67A to 97A.

Our fiscal year-end is October 31. All dollar amounts in management's discussion and analysis are in Canadian dollars, unless otherwise specified.

Overview

| TABLE 1 Net income | | | |
|--|----------|----------|----------|
| (\$ millions, except percentage amounts) | % change | 2002 | 2001 |
| Net income (1) | 15% | \$ 2,762 | \$ 2,411 |
| Impact of special items (2) | | — | (230) |
| Core net income | 27% | \$ 2,762 | \$ 2,181 |

(1) Net income includes goodwill amortization expense of \$246 million in 2001 (nil in 2002).
(2) Special items are shown in Table 6 on page 27A.

As shown in the tables above, full year net income increased \$351 million or 15% (12% on a per share basis). Excluding special items of \$230 million (\$36 per share) in 2001 detailed on page 27A, full year net income was up \$581 million or 27% and EPS were up 24%. Excluding special items and goodwill amortization expenses of \$246 million in 2001, net income was up \$335 million or 14% and EPS were up \$.39 or 11% in 2002 compared to 2001. This \$335 million growth was largely driven by a \$132 million increase in net income from recent U.S. acquisitions (excluding goodwill amortization expenses in 2001), cost savings of approximately \$165 million after-tax from operations other than our recent U.S. acquisitions and lower provisions for credit losses of approximately \$37 million after-tax.

On November 1, 2001, we adopted new accounting standards regarding business combinations under which goodwill is no longer amortized and is instead assessed for impairment at least annually. Accordingly, we did not incur goodwill amortization expense this year, whereas, in 2001, we incurred goodwill amortization expense of \$246 million after-tax (\$.38 per share).

Net income from our recent U.S. acquisitions was \$180 million in 2002, up from \$(114) million in 2001 (\$57) million excluding special items), partially reflecting the cessation of goodwill amortization this year, which accounted for \$105 million of the net income improvement.

| TABLE 2 Diluted earnings per share (EPS) | | | |
|--|----------|---------|---------|
| (\$, except percentage amounts) | % change | 2002 | 2001 |
| EPS (1) | 12% | \$ 3.93 | \$ 3.52 |
| Impact of special items (2) | | — | (.36) |
| Core EPS | 24% | \$ 3.93 | \$ 3.16 |

(1) EPS includes goodwill amortization expense of \$.38 per share in 2001 (nil in 2002).
(2) Special items are shown in Table 6 on page 27A.

Excluding special items and goodwill amortization expenses, recent U.S. acquisitions resulted in an increase in net income of \$132 million, largely reflecting the acquisition of Centura Banks, Inc. on June 5, 2001, which contributed seven more months of earnings in 2002 compared to 2001, synergies achieved from the integration of Tucker Anthony Sutro (acquired on October 31, 2001) into RBC Dain Rauscher, and stronger performance from RBC Dain Rauscher's fixed income business.

The lower growth rate in EPS than in net income reflected 32 million additional average common shares outstanding in 2002 as compared to last year. This largely reflects the issuance of common shares in last year's third quarter in connection with the share exchange for the acquisition of Centura Banks, partially offset by share repurchases during 2002.

As shown in Table 3 below, in 2002, U.S. and Other International revenues were \$5.8 billion or 37% of total revenues, up from \$4.2 billion or 28% in 2001. Recent U.S. acquisitions resulted in U.S. revenues increasing to \$4.3 billion or 27% of total revenues, from \$2.8 billion or 19% in 2001.

Total U.S. net income improved to \$154 million from \$(173) million in 2001 (\$(116) million excluding special items), despite higher provisions for credit losses this year, largely for the reasons described above.

| TABLE 3 Earnings by geographic segment | | | | | | | | |
|---|----------|---------------|---------------------|----------|----------|---------------|---------------------|----------|
| (\$ millions, taxable equivalent basis) | 2002 | | | | 2001 | | | |
| | Canada | United States | Other International | Total | Canada | United States | Other International | Total |
| Net interest income | \$ 5,556 | \$ 1,262 | \$ 380 | \$ 7,198 | \$ 5,614 | \$ 485 | \$ 450 | \$ 6,549 |
| Other income | 4,411 | 3,040 | 1,111 | 8,562 | 4,972 | 2,355 | 888 | 8,215 |
| Gross revenues | 9,967 | 4,302 | 1,491 | 15,760 | 10,586 | 2,840 | 1,338 | 14,764 |
| Provision for credit losses | 529 | 440 | 96 | 1,065 | 757 | 379 | (17) | 1,119 |
| Non-interest expense | 5,920 | 3,676 | 824 | 10,420 | 6,326 | 2,715 | 714 | 9,755 |
| Income taxes (1) | 1,432 | 32 | 49 | 1,513 | 1,537 | (81) | 23 | 1,479 |
| Net income | \$ 2,086 | \$ 154 | \$ 522 | \$ 2,762 | \$ 1,966 | \$ (173) | \$ 618 | \$ 2,411 |
| Core net income (2) | \$ 2,086 | \$ 154 | \$ 522 | \$ 2,762 | \$ 1,679 | \$ (116) | \$ 618 | \$ 2,181 |

(1) Includes non-controlling interest and taxable equivalent adjustment.

(2) Excludes special items in 2001, which are described in Table 6 on page 27A. There were no special items in 2002.

Outlook

We are targeting growth in diluted earnings per share of 10–15% and a return on common equity of 17–19% in fiscal 2003 based on the expectations that our cost management efforts will allow expenses to grow at a lower rate than revenues and that capital market activity will pick up somewhat in 2003.

Financial priorities

Revenue growth and diversification

In 2002, revenues increased 7%, primarily reflecting recent U.S. acquisitions. Operating, or core, revenues (i.e., excluding special items in 2001) increased 10%, also primarily reflecting recent U.S. acquisitions, and were higher than our objective of core revenue growth of 7–10%. Excluding recent U.S. acquisitions, operating revenues were flat. Detailed discussion follows on pages 38A to 41A.

Cost control

Non-interest expense increased 7% and operating non-interest expense (which excludes special items, the costs of Stock Appreciation Rights (SARs) and retention compensation associated with acquisitions) increased 8%, reflecting recent U.S. acquisitions. Operating expenses excluding recent U.S. acquisitions were down 5%. A full description is provided on pages 42A to 44A.

Strong credit quality

Provisions for credit losses and impaired loans declined this year despite further deterioration in the telecommunication sector. The specific provision for credit losses ratio was .51% (.49% net of effect of credit derivatives) in 2002 compared to .53% in 2001. During the year, net write-offs were .60% compared to .47% in 2001. Detailed discussion and tables are provided on pages 45A to 52A.

Balance sheet and capital management

Total assets were \$377 billion at October 31, 2002, up \$17.7 billion or 5% from October 31, 2001. At October 31, 2002, using Superintendent of Financial Institutions Canada (OSFI) guidelines and Canadian GAAP financial information, our Tier 1 capital ratio was 9.3% versus 8.7% at October 31, 2001, while the Total capital ratio was 12.7% versus 11.8% at October 31, 2001. Both ratios were above our medium-term (3–5 year) capital goals of 8% for Tier 1 capital and 11–12% for Total capital. More details are provided on pages 58A to 60A.

Factors that may affect future results

There are numerous factors, many beyond our control, that could cause results to differ significantly from our expectations. Some of these factors are described below. Other factors, including credit, market, liquidity, insurance, operational and other risks are described in the Risk management section beginning on page 53A.

By their very nature, and as noted in the "Caution regarding forward-looking statements" on page 21A, forward-looking statements involve inherent risks and uncertainties, both general and specific, and risks that predictions, forecasts, projections and other forward-looking statements will not be achieved. We caution readers not to place undue reliance on such statements in this management discussion and analysis as a number of important factors could cause actual results to differ materially from the plans, objectives, goals, targets, expectations, estimates and intentions expressed in such forward-looking statements.

Industry and non-company factors

As an integrated financial services company conducting business in Canada, the United States and other countries, our revenues and earnings are affected by the health of the economic, business and capital markets environments specific to the geographic regions in which we conduct business.

Factors such as interest rates, inflation, exchange rates, consumer spending, business investment, government spending, the health of the capital markets and terrorism impact the business and economic environment and, ultimately, the amount of business we conduct in a specific geographic region. For example, in an economic downturn characterized by higher unemployment, lower family income, lower corporate earnings, lower business investment and consumer spending, the demand for our loan and other products would be adversely affected and the provision for credit losses would likely increase, resulting in lower earnings. Similarly, a continuation or worsening of the current prolonged downturn in the equity markets could cause a further reduction in new issue and investor trading activity, assets under management (AUM), and assets under administration (AUA) resulting in lower fee, commission and other revenues.

Our earnings are affected by the monetary policies of the Bank of Canada and the Board of Governors of the Federal Reserve System in the United States.

Changes in the supply of money and the level of interest rates can impact our profitability. A decline in interest rates would result in a decrease in the net interest income earned on our non-trading portfolio and an increase in the value of our long principal positions of securities subject to interest rate risk. Conversely, an increase in interest rates would result in an increase in the net interest income earned on our non-trading portfolio and a decrease in the value of our long principal positions of securities subject to interest rate risk. For a more complete discussion of interest rate risk and its potential impact on our non-trading portfolio, please refer to the discussion of asset/liability management activities in our non-trading portfolio on page 61A. For a more complete discussion of interest rate risk and its potential impact on the value of principal position of securities subject to interest rate risk, please refer to the discussion of trading activities on page 55A.

Our performance can be influenced by the degree of competition in the markets in which we operate.

The competition for clients among financial services companies in the consumer and business markets in which we operate is intense. Customer loyalty and retention can be influenced by a number of factors, including relative service levels, the prices of products or services and changes in the attributes of a product or service. Customer loyalty and retention can also be compromised as a result of the client being "cross sold" by a competitor firm. Non-financial companies can provide consumers with the option to pay bills and transfer funds without involving banks. Such disintermediation could reduce fee revenues.

Changes in the statutes, regulations and regulatory policies that govern activities in our various business lines could impact our results.

Regulations are in place to protect the financial and other interests of our clients. Changes to statutes, regulations or regulatory policies, including changes in the interpretation or implementation of statutes, regulations or regulatory policies, could affect us by increasing the ability of competitors to compete with the products and services we provide. In addition, our failure to comply with applicable statutes, regulations or regulatory policies could result in sanctions and financial penalties by regulatory agencies that could adversely impact our reputation and earnings.

Although we take reasonable measures to ensure compliance with governing statutes, laws, regulations and regulatory policies in the jurisdictions in which we conduct business, there is no assurance that we will always be in compliance or deemed to be in compliance. Accordingly, it is possible that we could receive a judicial or regulatory body judgment that results in fines, damages and other costs that would have a negative impact on our earnings.

Company specific factors

Our financial performance will be influenced by our ability to execute our U.S. expansion and integration strategy.

The first phase of our U.S. expansion strategy entailed putting together the original building blocks by acquiring businesses largely in the personal and commercial banking, insurance and wealth management areas. The second phase entails building scale by adding to these original building blocks through additional strategic acquisitions, increasing revenues through greater market penetration, new product and service offerings, heightened marketing and sales initiatives and through more client referrals between the companies operating in our different business lines. The second phase also entails achieving cost synergies through the integration of the back office and head office functions of our business units. Although we regularly explore opportunities for strategic acquisitions of companies in our lines of business, there is no assurance that we will be able to continue to complete acquisitions on terms and conditions that satisfy our investment criteria. Further, although results to date have met or exceeded our targets, there is no assurance we will continue to achieve anticipated cost synergies from the integration of acquired companies. Our performance is contingent on retaining the clients and key employees of acquired companies, although there can be no assurance that we will always succeed in doing so.

Our business depends on attracting and retaining key employees.

Our success as an integrated financial services company depends to a large extent on our ability to attract and retain key employees. The competition for talented people in the financial services sector is intense. There is no assurance that we will be able to continue to attract and retain key employees, although our policies and practices are geared towards doing so and attrition at the management level is low.

Other factors

Other factors that may affect future results include changes in trade policy, the timely development and introduction of new products and services in receptive markets, changes in tax laws, technological changes, unexpected judicial or regulatory proceedings, unexpected changes in consumer spending and saving habits, the possible impact on our businesses of international conflicts and other developments including those relating to the war on terrorism, and our anticipation of and success in managing the risks implicated by the foregoing.

We caution that the foregoing discussion of factors that may affect future results is not exhaustive. When relying on forward-looking statements to make decisions with respect to Royal Bank of Canada, investors and others should carefully consider the foregoing factors, other uncertainties and potential events, and other external and company specific factors that may adversely impact future results and the market valuation placed on our common shares. We do not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by Royal Bank of Canada, or on our behalf.

Critical accounting policies

Our significant accounting policies are outlined in Note 1 on pages 72A to 75A. Certain of these policies require us to make estimates or assumptions that in some cases may relate to matters that are inherently uncertain. These policies include determining the allowance for credit losses, reporting the fair value of certain financial instruments, accounting for securitizations, determining the cost and obligations associated with pensions and postretirement benefits, and valuing goodwill and other intangibles.

Allowance for credit losses

The allowance for credit losses reflects management's estimate of probable losses in our loan and off-balance sheet portfolios at the balance sheet date. We determine and maintain an allowance based on a comprehensive and systematic review of our lending and off-balance sheet portfolios. As mentioned in Note 1 on page 73A, our evaluation focuses on identifying and evaluating problem accounts and estimating probable losses that may exist on the remaining portfolio.

Specific allowances are maintained to absorb losses on both specifically identified borrowers and other more homogeneous loans that have been recognized as impaired. The losses relating to identified large business and government debtors are estimated based on the present value of expected payments on an account-by-account basis. Management's judgment is required when forecasting the amount and timing of expected payments. The losses relating to other portfolio-type products, excluding credit cards, are based on historical net write-off experience. This amount represents the average percentage lost on impaired balances and is based on past history and management's judgment.

The general allocated allowance represents the best estimate of probable losses within the portfolio that have not been specifically identified as impaired. Estimates of portfolio losses are largely dependent on portfolio quality and economic conditions. In addition to the statistical analysis performed, management's judgment is required in determining the following inputs into the models employed:

- Expected default frequency
- Loss severity
- Write-off trends
- Economic conditions, including duration of current cycle

We determine and hold a general unallocated allowance, which explicitly reflects the subjective and judgmental elements involved in our determination of credit risk and the resulting loss estimates. In determining this allowance, management considers general economic and business conditions, regulatory requirements, recent loan loss experience and trends in credit quality and concentration.

The use of different estimates or assumptions in determining the allowance for credit losses may produce significantly different provisions for credit losses and financial results.

Fair value of financial instruments

We hold financial assets and liabilities, which are carried at fair value. These financial instruments comprise assets and liabilities held in our trading portfolio and derivative financial instruments. Fair value for a majority of financial instruments in our portfolios is determined based on quoted market prices and provides the best evidence of value since it is the result of two willing parties transacting in an open market. Note 21 on pages 94A and 95A contains accounting disclosure regarding the estimated fair value of financial instruments.

If quoted market prices are not available for certain assets or liabilities, we use financial valuation models to determine fair value. A provision is made in situations where we believe there is the potential the amount realized on sale will be less than the estimated fair value due to insufficient liquidity over a short period of time. We also maintain a provision for model risk, which may occur when the estimated value does not reflect the true value under certain stress market conditions. All significant financial valuation models are vetted by our risk management function, which is not involved in trading the assets and liabilities and is able to provide an independent perspective. Our internal financial valuation models for accounting are strictly controlled and regularly recalibrated, and require the approval of our risk management function. The assumptions used in the financial models are subject to management's judgment, and different assumptions may produce significantly different fair values and financial results.

As outlined in Note 1 on page 72A, changes in the fair value of trading account assets and liabilities are recognized in earnings. Writedowns to reflect permanent impairment are recognized in earnings. We regularly assess whether permanent impairment exists.

For derivative financial instruments, we determine fair value using various methodologies including quoted market prices, prevailing market values for similar instruments, and net present value of future cash flows and other pricing models. In determining the assumptions used in our pricing and valuation models, where appropriate, we look to external market inputs including factors such as interest rate yield curves, currency rates and price and rate volatilities for options and other derivatives. The use of methodologies, models and assumptions in pricing and valuing derivatives is subjective and requires management's judgment. The use of different methodologies, models and assumptions may result in significantly different fair values and financial results.

Securitizations

Securitization is a process by which we sell loans or other financial assets to a special purpose entity (SPE), which funds the purchase by issuing securities to investors. The return to investors is derived from the cash flows of the loans or other financial assets purchased by the SPE. Details of our securitization activities are contained in Note 7 on page 81A. A discussion of our involvements with SPEs can be found on pages 64A and 65A.

The calculation of the gain or loss on our securitization transactions involves the use of estimates and assumptions including expected credit losses, payment rates, discount rates and estimated future excess spread. The use of different estimates and assumptions may produce significantly different results reported in earnings.

Pensions and postretirement benefits

We offer various pension plans and postretirement benefit plans to our employees. Note 15 on page 87A contains accounting disclosure concerning our obligations with respect to these plans. The determination of obligations under our pension and other postretirement plans and related expense requires the use of actuarial valuation methods and assumptions. Assumptions typically used in determining these amounts include, as applicable, mortality rates, rate of employee turnover, future claims costs, discount rates, future salary and benefit levels, return on plan assets and future medical costs. The fair value of plan assets is determined using market values or approximations of market values for assets where market values are not readily available. Actuarial valuations and the determination of certain market value approximations are subject to management judgment and, as a result, the prepaid benefit asset (obligation) and pension and postretirement expense may differ significantly if different assumptions are used.

Goodwill and other intangibles

As outlined in Note 4 on page 78A, we adopted the Canadian Institute of Chartered Accountants (CICA) standard on *Goodwill and Other Intangibles Assets*. Under this accounting standard, goodwill is no longer amortized but is tested at least annually for impairment at the reporting unit level. Impairment is determined by comparing the fair value of a reporting unit to its carrying value. The fair value of a reporting unit and assets and liabilities within a reporting unit may be determined using a number of market valuations methods including quoted market prices, discounted cash flows and net realizable values. Inherent in each of these valuation techniques is the use of assumptions and estimates. Both the valuation method and the assumptions and estimates used therein are based on management's judgment. The use of different judgments and estimates may produce significantly different results in applying the goodwill impairment test.

Economic Profit

In addition to using traditional measures of financial performance such as net income, EPS and return on common equity (ROE), we also evaluate our performance based on the amount of Economic Profit earned. Economic Profit measures each business segment's cash operating earnings after providing for the cost of capital committed to the segment.

Cash operating earnings is net income available to common shareholders excluding the after-tax impact of special items and amortization of goodwill and other intangibles. The equity capital charge is derived by applying the cost of common equity, which is our proxy for the after-tax return required by shareholders for the use of their capital, to the amount of average common equity, commonly referred to as Economic Capital (EC). The estimated cost of equity is reviewed annually. As the result of a decline in longer-term bond yields since the last review, the cost of common equity was reset mid-year to 11.5% from 12.5%. The average cost of common equity in 2002 was 12%.

Economic Profit does not have any standardized meaning prescribed by GAAP, and therefore the Economic Profit information that we provide is unlikely to be comparable to similar measures presented by other companies. We present information on an Economic Profit basis as it is used by our management and because some investors may also find it useful in evaluating our financial performance and analyzing trends in our businesses.

To create shareholder value from an Economic Profit point of view, one must generate cash operating earnings in excess of the common equity capital charge. Positive Economic Profit adds to shareholder value while negative Economic Profit erodes shareholder value.

Economic Profit measures the change in value created for shareholders over time, and we believe it is an effective planning tool to focus attention on shareholder value growth opportunities. In order to maximize Economic Profit, one must seek to:

- Increase cash operating earnings without tying up more capital
- Target investments in projects that yield positive economic returns
- Improve overall effectiveness of invested capital through re-allocation from less effective uses
- Improve the risk-return profiles of the lines of business

We believe that Economic Profit analysis strengthens risk management discipline, as business segments are attributed capital based on their credit, market, operational and other risks. This discipline has resulted in controlled growth and a focus on returns commensurate with risks. Furthermore, Economic Profit encourages redistribution of resources from weaker to stronger performing businesses.

As shown in Table 4 below, we had Economic Profit of \$712 million in 2002, up from \$539 million in 2001. This increase is the result of cash operating earnings growing at a faster rate than the capital charge. The Economic Profit amounts for the business segments in 2002 and 2001 are shown in the tables on pages 28A, 30A, 32A, 34A and 36A.

TABLE 4 Economic Profit (1)

| (\$ millions, except percentage amounts) | 2002 | 2001 | 2000 | 1999 | 1998 |
|---|-----------|-----------|-----------|-----------|----------|
| Net income available to common shareholders | \$ 2,664 | \$ 2,276 | \$ 2,140 | \$ 1,600 | \$ 1,679 |
| Adjustment for special items (after-tax) | — | (230) | — | 102 | 3 |
| Adjustment for amortization of goodwill and other intangibles (after-tax) | 64 | 282 | 84 | 63 | 62 |
| Cash operating earnings | 2,728 | 2,328 | 2,224 | 1,765 | 1,744 |
| Capital charge | (2,016) | (1,789) | (1,460) | (1,386) | (1,229) |
| Economic Profit (1) | \$ 712 | \$ 539 | \$ 764 | \$ 379 | \$ 515 |
| Economic Profit growth | 32% | (29)% | 102% | (26)% | 8% |
| Average common equity | \$ 16,809 | \$ 13,843 | \$ 10,814 | \$ 10,264 | \$ 9,107 |
| Cost of common equity (2) | 12.0% | 12.9% | 13.5% | 13.5% | 13.5% |

(1) Economic Profit is cash operating earnings (i.e., net income available to common shareholders excluding the after-tax impact of special items and amortization of goodwill and other intangibles) less a charge for the cost of common equity.

(2) Average for the year.

Line of business results

Overview

Table 5 on page 27A shows our results by business segment in 2002. Our 2001 results include several special items, shown in Table 6 and described below. There were no special items in 2002.

Special items increased net income by \$230 million in 2001. There were three items that increased other income – an \$89 million gain on the formation of the Moneris Solutions merchant card processing joint venture with Bank of Montreal, a \$43 million gain on the sale of the Group Retirement Services group pension benefits administration business and a \$313 million gain on the sale of RT Capital Management's institutional money management business. Non-interest expense increased due to a \$91 million restructuring charge related to integration and cost-saving initiatives in the U.S. retail banking platform. Income taxes were increased by a tax expense of \$75 million, reflecting a write-down of deferred tax assets due to reductions in tax rates.

We attribute common equity to our business segments based on an assessment of their credit, market, operational and other risks. Common equity in the Other segment includes equity attributed to specific functional units that are reported in Other, as well as any differences between our total common equity and common equity attributed to our businesses or our functional units. We implemented a number of changes to refine our capital attribution methodologies in early 2002, resulting in higher common equity being attributed to RBC Capital Markets and RBC Investments and lower common equity to RBC Banking and RBC Insurance compared to a year ago. However, the inclusion of a full year of operations of RBC Centura Bank in 2002, as compared to 2001, resulted in more common equity being attributed to RBC Banking. The amount of common equity attributed to the Other segment increased in 2002, largely as the result of internal capital generation outstripping the need to attribute additional common equity to the other five segments, based on an assessment of their risk profiles. Our attribution of capital to the business segments involves various assumptions and judgments.

RBC Banking produced an ROE of 19.1% and generated 55% of our net income in 2002. Net income increased 30% from 2001 and core net income (net income excluding the special items in Table 6) increased \$266 million or 21%, as discussed on page 28A. This improvement partially reflected higher core earnings from U.S. acquisitions (which include RBC Centura acquired on June 5, 2001, and RBC Mortgage), which rose to \$195 million from \$21 million (\$73 million excluding goodwill amortization expense) a year ago.

RBC Insurance produced an ROE of 15.7% and generated 4% of our net income in 2002. Net income declined 12% from 2001, as discussed on page 30A. RBC Liberty Insurance (acquired on November 1, 2000) reported a net loss of \$18 million in 2002 compared to a loss of \$5 million (net income of \$8 million excluding goodwill amortization expense) in 2001.

RBC Investments produced an ROE of 11.0% and generated 12% of our net income in 2002. Net income declined by 33% while core net income increased \$104 million or 44%, as discussed on page 32A. RBC Dain Rauscher (acquired on January 10, 2001) made a profit of \$3 million in 2002 compared to a loss of \$73 million (\$33 million excluding goodwill amortization) last year.

RBC Capital Markets produced an ROE of 10% and generated 15% of our net income in 2002. Net income increased 24% and core net income increased 15%, as discussed on page 34A.

RBC Global Services produced an ROE of 28.4% and generated 6% of our net income in 2002. Net income declined by 35% while core net income declined by 8%, as discussed on page 36A.

The Other segment produced an ROE of 24.4% and generated 8% of our net income in 2002. Its 2001 results are shown in Note 3 on page 77A. Gains from the securitization of mortgages contributed to the growth in earnings.

TABLE 5 Results by business segment

| (\$ millions, taxable equivalent basis, except per share and percentage amounts) | 2002 | | | | | | | 2001 | |
|--|-------------|---------------|-----------------|---------------------|---------------------|-----------|----------|----------|----------|
| | RBC Banking | RBC Insurance | RBC Investments | RBC Capital Markets | RBC Global Services | Other (1) | Total | Core | Reported |
| Net interest income | \$ 5,576 | \$ 223 | \$ 371 | \$ 553 | \$ 137 | \$ 338 | \$ 7,198 | \$ 6,549 | \$ 6,549 |
| Other income | 2,073 | 285 | 3,274 | 2,112 | 820 | (2) | 8,562 | 7,770 | 8,215 |
| Gross revenues | 7,649 | 508 | 3,645 | 2,665 | 957 | 336 | 15,760 | 14,319 | 14,764 |
| Provision for credit losses | 626 | — | (1) | 465 | 10 | (35) | 1,065 | 1,119 | 1,119 |
| Non-interest expense | 4,528 | 437 | 3,146 | 1,627 | 668 | 14 | 10,420 | 9,664 | 9,755 |
| Income taxes | 937 | (46) | 157 | 135 | 108 | 74 | 1,365 | 1,216 | 1,340 |
| Non-controlling interest | 8 | — | — | — | — | 100 | 108 | 107 | 107 |
| Taxable equivalent adjustment | 19 | — | — | 21 | — | — | 40 | 32 | 32 |
| Net income | \$ 1,531 | \$ 117 | \$ 343 | \$ 417 | \$ 171 | \$ 183 | \$ 2,762 | \$ 2,181 | \$ 2,411 |
| Net income | | | | | | | | | |
| As a % of total | 55% | 4% | 12% | 15% | 6% | 8% | 100% | 100% | 100% |
| % growth over prior year | 30% | (12)% | (33)% | 24% | (35)% | n.m. | 15% | (4)% | 6% |
| % core growth over prior year | 21% | (11)% | 44% | 15% | (8)% | n.m. | 27% | | |
| ROE | 19.1% | 15.7% | 11.0% | 10.0% | 28.4% | 24.4% | 15.8% | 14.8% | 16.4% |
| Economic Profit (2) | \$ 599 | \$ 27 | \$ (17) | \$ (76) | \$ 98 | \$ 81 | \$ 712 | \$ 539 | \$ 539 |
| Diluted EPS | | | | | | | \$ 3.93 | \$ 3.16 | \$ 3.52 |

(1) Represents other activities, which mainly comprise Corporate Treasury, Corporate Resources, Systems & Technology and Real Estate Operations.

(2) Economic Profit is cash operating earnings (i.e., net income available to common shareholders excluding the after-tax impact of special items and amortization of goodwill and other intangibles) less a charge for the cost of common equity.

n.m. not meaningful

TABLE 6 Special items affecting business segment results in 2001 (1)

| (\$ millions, taxable equivalent basis, except per share amounts) | RBC Banking | RBC Insurance | RBC Investments | RBC Capital Markets | RBC Global Services | Other (2) | Total |
|---|-------------|---------------|-----------------|---------------------|---------------------|-----------|--------|
| Other income | | | | | | | |
| Gain on formation of Moneris Solutions joint venture | \$ — | \$ — | \$ — | \$ — | \$ 89 | \$ — | \$ 89 |
| Gain on sale of Group Retirement Services | 7 | — | 36 | — | — | — | 43 |
| Gain on sale of RT Capital Management | — | — | 313 | — | — | — | 313 |
| | 7 | — | 349 | — | 89 | — | 445 |
| Non-interest expense | | | | | | | |
| U.S. retail banking restructuring charge | 91 | — | — | — | — | — | 91 |
| Total impact (pre-tax) | (84) | — | 349 | — | 89 | — | 354 |
| Income taxes | | | | | | | |
| On items listed above | (33) | — | 70 | — | 12 | — | 49 |
| Enactment of change in tax rates | 33 | (2) | 5 | 28 | — | 11 | 75 |
| Total impact (after-tax) | \$ (84) | \$ 2 | \$ 274 | \$ (28) | \$ 77 | \$ (11) | \$ 230 |
| Impact on diluted EPS | | | | | | | \$.36 |

(1) There were no special items at all in 2002.

(2) Represents other activities, which mainly comprise Corporate Treasury, Corporate Resources, Systems & Technology and Real Estate Operations.

RBC Banking

Business profile

RBC Banking serves over 11 million individuals, small and medium-sized businesses, and mid-market commercial clients in Canada, the U.S., the Caribbean and the Bahamas. Our distribution capabilities include a network of branches, business banking centres and other sales units, accredited financial planners, mobile sales representatives, automated banking machines, and telephone and Internet banking channels. We deliver a wide range of financial services including, deposit accounts, investments and mutual funds, financial planning and advice, credit and debit cards, business and personal loans, and residential and commercial mortgages.

Industry profile

In Canada, personal and commercial banking is a mature industry dominated by the five largest Canadian banks, although competition is fierce and niche players are increasing their presence in select businesses such as credit cards. The U.S. market is more fragmented, although many regional markets are highly competitive. Many banks have expanded their focus to include offering investment products and financial advice and planning to affluent and other targeted clients. Critical success factors, in our opinion, include providing a differentiated client experience and maintaining rigorous credit and operational risk management practices and expense control.

Our strengths

- Customer relationship management (CRM) combined with strong client contact capabilities and specialized sales forces
- Established Canadian retail banking brand
- Comprehensive product, service and physical and alternative distribution capabilities compared to niche players
- Highest client household penetration ratio in personal segments, and lead product market share in business markets among Canadian banks
- Among the strongest efficiency ratios of the Big 5 Canadian banks
- Acquisition integration capabilities in the U.S. market

Our strategy

Our vision is to grow profitable relationships with each one of our business and personal clients by creating a tailored client experience for our clients across North America, while reducing costs, and effectively managing risk and capital.

We plan to achieve our vision through the following strategic priorities:

- Ensure strong revenue growth in Canada by maximizing client retention, deepening client relationships, capturing intergenerational wealth transfer opportunities and building on our financial planning and advice capabilities
- Create a differentiated customer experience, providing a valued and superior level of service tailored to customer segment needs that builds customer loyalty and clearly differentiates us from the competition
- Accelerate U.S. revenue and earnings growth by expanding our footprint in the southeastern U.S. and building a scalable platform
- Reinforce cost management and risk mitigation through effective use of technology, strengthened low cost delivery capabilities, and rigorous management of credit, operational, regulatory and compliance risk
- Cross-platform leverage by increasing referrals and cost efficiencies across RBC in Canada and the U.S.

Outlook for 2003

Based on our expectation of rising interest rates in Canada in 2003, we anticipate that the spread compression on deposits will ease. This, combined with reasonable loan growth, should have positive implications for revenue growth in our Canadian business. In the U.S., we anticipate branch openings and the acquisitions of Eagle Bancshares in July 2002 and of Admiralty Bancorp, Inc. (expected to close in January 2003) to have a positive impact on revenues. We also expect that the realization of a full year of cost synergies from the Eagle Bancshares acquisition will contribute to net income growth at RBC Centura. Overall, we expect solid earnings growth for this segment based on our continued focus on cost containment and credit and operational risk management and the benefits of a recovering economy.

Financial performance

Net income was up 30% from last year while core net income was up \$266 million or 21%. Earnings from the segment's U.S. acquisition rose to \$195 million in 2002 from \$(36) million last year or \$21 million, excluding costs related to U.S. retail bank restructuring in 2001 (\$73 million further excluding goodwill amortization expense in 2001). The higher U.S. earnings reflected the acquisition of Centura Banks on June 5, 2001, integration cost savings and revenue growth. Core net income excluding U.S. acquisitions grew 7% due to continued cost management initiatives. Core ROE increased to 19.1% in 2002 from 18.2% despite higher average common equity attributed to this segment due to U.S. acquisitions and additional business activity.

Revenues increased \$431 million or 6% from 2001, reflecting the contribution of RBC Centura (including RBC Mortgage) and the acquisition of Eagle Bancshares, which was completed on July 22, 2002. Revenues from U.S. acquisitions increased \$617 million in 2002, without which the segment's revenues would have decreased 3% due to narrower net interest margins and lower lending volumes.

Non-interest expense increased \$139 million or 3% from last year, while the efficiency ratio declined 160 basis points, as revenues grew faster than expenses. Core non-interest expense (which excludes \$91 million of costs related to U.S. retail bank restructuring in 2001) increased \$230 million or 5%. U.S. acquisitions contributed \$330 million of the core expense growth. Excluding U.S. acquisitions, core expenses fell 3%, reflecting ongoing cost management.

The total provision for credit losses fell 14% from last year, largely in the commercial loan portfolio. Net impaired loans decreased by \$92 million, reflecting improvements in both the Canadian consumer and Canadian commercial loan portfolios.

Results

| (\$ millions, taxable equivalent basis, except percentage amounts) | % change | 2002 | 2001 |
|--|----------|------------|------------|
| Net interest income | 4% | \$ 5,576 | \$ 5,349 |
| Other income | 11 | 2,073 | 1,869 |
| Gross revenues | 6 | 7,649 | 7,218 |
| Provision for credit losses | | | |
| Allocated specific | (5) | 626 | 662 |
| General allocated and unallocated | n.m. | - | 70 |
| Total | (14) | 626 | 732 |
| Non-interest expense (1) | 3 | 4,528 | 4,389 |
| Net income before income taxes | 19 | 2,495 | 2,097 |
| Income taxes | 4 | 937 | 900 |
| Non-controlling interest | (20) | 8 | 10 |
| Taxable equivalent adjustment | 217 | 19 | 6 |
| Net income | 30 | \$ 1,531 | \$ 1,181 |
| U.S. net income | n.m. | \$ 195 | \$ (36) |
| Net income as a % of | | | |
| total bank net income | 600 bp | 55% | 49% |
| ROE | 220 bp | 19.1% | 16.9% |
| Economic Profit | 45% | \$ 599 | \$ 412 |
| Net interest margin | (18)bp | 3.56% | 3.74% |
| Efficiency ratio | (160)bp | 59.2% | 60.8% |
| Operating efficiency ratio (2) | (50)bp | 59.0% | 59.5% |
| Average assets | 9% | \$ 156,500 | \$ 143,100 |
| Average loans and acceptances | 6 | 142,800 | 134,900 |
| Average deposits | 10 | 122,900 | 111,400 |
| Average common equity | 16 | 7,800 | 6,700 |
| Core results (3) | | | |
| Gross revenues | 6 | 7,649 | 7,211 |
| Non-interest expense | 5 | 4,528 | 4,298 |
| Net income | 21 | 1,531 | 1,265 |
| U.S. net income | 829 | 195 | 21 |
| ROE | 90 bp | 19.1% | 18.2% |
| Credit information | | | |
| Net impaired loans | n.m. | \$ (305) | \$ (213) |
| Net write-offs | 3% | 744 | 724 |
| Net write-offs as a % of | | | |
| average loans and acceptances | (2)bp | .52% | .54% |
| Number of employees | | | |
| (full-time equivalent) | - | 35,014 | 34,845 |

(1) Includes goodwill amortization expense of \$54 million in 2001 (nil in 2002).

(2) Efficiency and operating efficiency ratios are defined on page 104.

(3) Excluding special items in 2001 detailed in Table 6 on page 27A. Only the lines affected by special items are shown here.

n.m. not meaningful

Strategy by division

Canada

Operating in Canada under the RBC Royal Bank brand, we serve individuals, small and medium-sized businesses, and commercial clients in all provinces and territories. We offer our clients extensive physical and alternative distribution choices. We continue to strengthen our channel distribution capabilities, including significant reinvestment in our branch network and staff, and in our electronic banking capabilities.

We offer a wide range of financial services and advice, as detailed in our business profile on page 28A, and products and expertise in specialized areas such as foreign exchange and venture capital financing. We also provide individual and business clients with a full choice of Visa credit card products, debit cards and other smart card applications. We provide merchants with credit and debit card acceptance services, point-of-sale capabilities and Internet-secure electronic transaction solutions through Moneris Solutions, a joint venture in which we participate equally with Bank of Montreal, managed through RBC Global Services.

Our goal is to grow profitable relationships with each one of our business and personal clients, using our expertise in customer relationship management, sales management and client segmentation. We will drive revenue growth by creating a tailored client experience, leveraging client life events and providing financial planning and advice to broaden client relationships using the full capabilities of RBC.

We will continue to reinforce our cost management focus by leveraging e-enabled technology and cross-platform economies of scale. We will continue to rigorously focus on the management of credit, operational and compliance risk, including fraud management initiatives and strengthened credit-scoring capabilities.

United States

RBC Centura serves as the focal point of our personal and commercial banking businesses in the U.S. Headquartered in Rocky Mount, North Carolina, RBC Centura serves individual and business clients in the southeastern U.S. RBC Centura also includes RBC Mortgage, a Chicago-based national retail mortgage originator, and RBC Builder Finance, a Houston-based financing division for home builders and developers. RBC Centura's footprint expanded in 2002 with the acquisition of Eagle Bancshares, which operated 14 branches in the Atlanta, Georgia metropolitan area. RBC Centura has also announced a definitive merger agreement with Admiralty Bancorp, which currently operates 10 branches in Florida, expected to close in January 2003.

Our U.S. priorities include:

- Expanding in the southeastern U.S. through targeted acquisitions and a build/buy branch expansion strategy
- Rapidly building a scalable platform to support growth
- Accelerating introduction of sales and marketing initiatives
- Growing national niche lines of business such as builder finance and residential mortgages
- Realizing synergies from functional integration and cross-selling opportunities across RBC's entire platform

Caribbean and the Bahamas

Operating under the brand name RBC Royal Bank of Canada, we provide a broad range of personal and commercial banking products and services to individual and business clients in the Bahamas, Barbados, the Cayman Islands and Eastern Caribbean Islands through a network of branches and automated banking machines.

Financial highlights by division

Revenues from the domestic business decreased \$196 million or 3% from 2001, primarily due to continued spread compression on core deposits and lower personal and business lending volumes. These decreases more than offset higher residential mortgage and deposit balances and wider net interest margin earned on mortgages and credit cards. Mortgage balances increased as the low interest rate environment encouraged home purchases. Deposit balances grew while lending volumes declined, reflecting consumer and business uncertainty regarding the economy and capital markets.

Results

| (\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|-----------|-----------|
| Gross revenues | (3)% | \$ 6,110 | \$ 6,306 |
| Average residential mortgages | 5 | 68,200 | 64,800 |
| Average personal loans | (4) | 23,600 | 24,500 |
| Average personal deposits | 2 | 74,400 | 72,900 |
| Average business loans and acceptances | (8) | 32,700 | 35,600 |
| Average business deposits | 9 | 30,500 | 28,100 |
| Average card balances | 3 | 6,200 | 6,000 |
| Card spending volumes | 2 | 26,700 | 26,300 |
| Number of: | | | |
| Employees (full-time equivalent) | 1 | 29,716 | 29,554 |
| Automated banking machines | (2) | 4,151 | 4,236 |
| Branches | (1) | 1,117 | 1,125 |
| Online clients | 23 | 2,311,915 | 1,876,358 |

Revenues increased \$617 million due mainly to a full year of RBC Centura results in 2002 compared to 5 months in 2001, as well as the contribution of Eagle Bancshares since July 22, 2002. Growth in average balances also largely reflects the inclusion of a full year of RBC Centura. Strong growth in mortgage originations and volumes at RBC Mortgage reflected high refinancing activity resulting from the favourable interest rate environment.

Results

| (\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|----------|--------|
| Gross revenues | 91% | \$ 1,296 | \$ 679 |
| Average residential mortgages | 81 | 2,900 | 1,600 |
| Average personal loans | 154 | 3,300 | 1,300 |
| Average personal deposits | 121 | 8,600 | 3,900 |
| Average business loans and acceptances | 121 | 8,600 | 3,900 |
| Average business deposits | 93 | 5,400 | 2,800 |
| Average card balances | — | 100 | 100 |
| Card spending volumes | 100 | 400 | 200 |
| Mortgage originations (\$ billions) | 50 | 33.7 | 22.5 |
| Number of: | | | |
| Employees (full-time equivalent) | 1 | 4,181 | 4,126 |
| Automated banking machines | 7 | 275 | 258 |
| Branches (1) | 1 | 245 | 242 |
| Online clients | 18 | 89,434 | 75,887 |

(1) Excludes RBC Mortgage and RBC Builder Finance sales offices of 252 in 2002 and 264 in 2001.

Revenues increased \$10 million or 4% from 2001, aided by the sale of property in the Cayman Islands, which accounted for approximately half of the increase.

Results

| (\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|--------|--------|
| Gross revenues | 4% | \$ 243 | \$ 233 |
| Number of: | | | |
| Employees (full-time equivalent) | (4) | 1,117 | 1,165 |
| Automated banking machines | 11 | 60 | 54 |
| Branches | 10 | 43 | 39 |

RBC Insurance

Business profile

Operating as RBC Insurance, we provide a wide range of creditor, life, health, travel, home, auto and reinsurance products and services to more than five million clients in Canada, the U.S. and internationally. These products and services are offered through a wide variety of distribution channels, including the telephone, independent brokers, travel agents, a proprietary sales force and the Internet.

Industry profile

The Canadian insurance industry generates almost \$60 billion in premiums annually from more than 100 life insurance companies and more than 200 property and casualty insurers. Our U.S. business is focused in the life insurance sector, which is both competitive and fragmented and includes over 1,200 national and regional companies. The international reinsurance industry is dominated by several global players but also includes a number of niche companies.

Across all of our business lines, we are seeing a number of key trends, including consolidation, increased government regulation, shifting distribution opportunities, the convergence of insurance and investment products and increased globalization.

Our strengths

- A diverse set of products designed to meet a wide range of consumer needs
- Multiple distribution channels, which are supported by strong infrastructure and sales expertise
- A strong brand. As part of RBC Financial Group, we have access to a broad range of financial services, distribution channels and client base
- Market leadership in a number of Canadian insurance markets, including travel and individual life insurance

Our strategy

We are focused on growing our insurance organization by offering a wide range of products and services through multiple distribution channels in Canada, as well as in select U.S. and international markets. To accomplish this we will seek to:

- Ensure as many RBC clients as possible have an insurance relationship with RBC Insurance
- Target reinsurance activities that support and enhance the overall profitability of the insurance operations
- Continue to expand in the U.S. by utilizing existing scale and expanding the platform, entering new markets and focusing on cross-platform initiatives across RBC
- Build an integrated North American insurance platform by leveraging cross-border synergies where permitted, including the implementation of common administrative and technology systems

Outlook for 2003

Our expectation of reasonable economic growth in both Canada and the U.S. should have a favourable impact on the insurance business in 2003. Our outlook is for strong revenue growth across our operations, driven by expansion into new markets as discussed in our strategy, and the pending acquisition of the U.S. life insurance operation of Business Men's Assurance Company of America (BMA). The acquisition of BMA is subject to regulatory approvals and other customary closing conditions. We anticipate that cost reductions from the realization of cross-border synergies will also help to drive net income growth.

Financial performance

Net income was \$117 million, down 12% from last year. Results in 2002 were adversely affected by a declining interest rate environment and weaker equity markets. RBC Liberty Insurance reported a loss of \$18 million versus a loss of \$5 million in 2001, (net income of \$8 million excluding goodwill amortization) last year. The decline in RBC Liberty Insurance earnings was largely related to higher policy surrenders and lower earnings at its outsourcing divisions. Excluding RBC Liberty Insurance, core net income fell 1%.

Core ROE improved to 15.7% from 14.8% in 2001, reflecting lower average common equity, which reflected a revised methodology for attributing capital to our insurance operations.

Premiums & deposits were up 12% from last year due largely to the contribution of RBC Liberty Insurance, while revenues increased 6% reflecting growth in the reinsurance business. RBC Liberty Insurance reported 13 months of results in 2002 versus 11 months in 2001, as its reporting period was changed from September 30 to October 31 to be consistent with our fiscal year. Excluding the additional months of RBC Liberty Insurance, premiums & deposits grew 8% and revenues declined 1%.

Expenses grew \$62 million or 17%, largely due to the two additional months of RBC Liberty Insurance and an increase in the number of employees, partly offset by the cessation of goodwill amortization this year. Excluding the additional months of RBC Liberty Insurance, expenses increased 7%.

Results

| (\$ millions, except percentage amounts) | % change | 2002 | 2001 |
|--|----------|----------|----------|
| Premiums & deposits | 12% | \$ 2,023 | \$ 1,812 |
| Other income | | | |
| Earned premium | 14 | 1,767 | 1,548 |
| Fee revenue/Other | (16) | 109 | 130 |
| Less: Policy benefits | 19 | 1,253 | 1,054 |
| Less: Acquisition costs | (3) | 338 | 350 |
| | 4 | 285 | 274 |
| Net interest income | 8 | 223 | 206 |
| Gross revenues | 6 | 508 | 480 |
| Non-interest expense (1) | 17 | 437 | 375 |
| Net income before income taxes | (32) | 71 | 105 |
| Income taxes | n.m. | (46) | (28) |
| Net income | (12)% | \$ 117 | \$ 133 |
| U.S. net income | (250) | \$ (6) | \$ 4 |
| Net income as a % of total bank net income | (200)bp | 4% | 6% |
| ROE | 70 bp | 15.7% | 15.0% |
| Economic Profit | (10)% | \$ 27 | \$ 30 |
| Average assets | 6 | 5,600 | 5,300 |
| Average common equity | (12) | 700 | 800 |
| Core results (2) | | | |
| Net income | (11) | 117 | 131 |
| ROE | 90 bp | 15.7% | 14.8% |
| Number of employees (full-time equivalent) | 2% | 2,641 | 2,583 |

(1) Includes goodwill amortization expense of \$13 million in 2001 (nil in 2002).
(2) Excluding special items in 2001 detailed in Table 6 on page 27A. Only the lines affected by special items are shown here.

Strategy by division

Life

Our life business provides a wide range of individual and group life and health insurance products to both individual and business clients in Canada and the U.S., as well as life reinsurance and retrocession to businesses around the world.

In Canada, life and health insurance products are distributed through a network of more than 7,000 independent brokers, over 550 proprietary insurance representatives and a direct sales unit. In the U.S., Greenville, South Carolina-based Liberty Life Insurance Company provides life and health insurance products through a proprietary sales force of over 600 agents and also offers select products through direct channels.

Our goal is to continue to grow our life businesses by expanding our client base and range of products and services offered, as well as by enhancing our distribution networks.

Non-life

Our non-life business includes home, auto, travel and property reinsurance for individual and business clients in Canada and select international markets.

We provide Canadians with a wide range of auto and home insurance products, offering them to individual clients and employee and affinity groups through direct sales and face-to-face channels. Travel products, which are sold through travel agents, the Internet and bank channels in Canada, include trip cancellation insurance, out-of-country medical and baggage insurance.

We participate in the property reinsurance business by accepting a share of the risk on property policies issued by other insurance companies. The majority of our current business is generated from insurance companies in the U.S. and Europe.

Our goal is to grow our non-life business by continuing to build our domestic home and auto business, entering new travel insurance markets and effectively managing our property reinsurance portfolio.

Fee businesses

We are involved in a number of other key insurance and related activities that generate fee income, including travel assistance services, structured reinsurance, the administration of bank creditor insurance programs and a proprietary sales distribution network.

Our travel and emergency assistance services include co-ordinating the delivery of emergency health, evacuation and transportation services when clients have a travel emergency, while our structured reinsurance business provides solutions to help corporations better manage financial risk.

In the U.S., our fee businesses include outsourcing services and administration and software systems provided through Liberty Insurance Services Corporation (LIS). The Business Process Outsourcing division of LIS provides services such as underwriting, billing and collection, and claims processing for nearly 4 million policies under administration. The Software Solutions division develops Web-enabled software for life, health, annuity and reinsurance administration. Together, these divisions have more than 200 client sites and serve domestic, international and multinational insurers worldwide.

Our goal is to continue to leverage our existing infrastructure and technology to enhance existing programs and grow these businesses.

Financial highlights by division

Premiums & deposits for the life business increased 10% in 2002, partially due to 2 additional months of RBC Liberty Insurance as it reported 13 months of results in 2002 versus 11 months in 2001. Without these additional months, premiums & deposits would have been up 5%, reflecting the continued strength of both the Canadian and reinsurance businesses. Lower investment income due to the low interest rate environment, as well as higher policy surrenders at RBC Liberty Insurance, contributed to the 7% decline in revenues.

Results

| (\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|----------|----------|
| Premiums & deposits | 10% | \$ 1,529 | \$ 1,393 |
| Gross revenues | (7) | 362 | 388 |
| Average assets | 2 | 4,400 | 4,300 |
| Number of: | | | |
| Life and health policies in force in Canada (thousands) | 11 | 2,930 | 2,645 |
| Life policies in force in the U.S. (thousands) | (11) | 2,325 | 2,600 |
| Assets under management in the U.S. | (2) | 367 | 375 |
| U.S. sales agents | (4) | 690 | 718 |

Revenues from our non-life business were higher in 2002 due to stronger performance in our property reinsurance and travel businesses as last year's revenues were adversely affected by claims resulting from the World Trade Center tragedy.

Results

| (\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|--|----------|--------|--------|
| Premiums & deposits | 14% | \$ 413 | \$ 363 |
| Gross revenues | 80 | 45 | 25 |
| Average assets | — | 700 | 700 |
| Number of: | | | |
| Home and auto – personal lines policies in force (thousands) | 37 | 93 | 68 |
| Travel – coverages (thousands) | (7) | 2,339 | 2,510 |

The substantial growth in premiums & deposits was attributable to structured reinsurance premium increases, which offset slower growth at our outsourcing divisions in the U.S. The increase in revenues reflected the stronger performance in structured reinsurance and the reporting of two additional months of RBC Liberty Insurance. Our career sales force grew substantially in 2002, reflecting increased investment in our proprietary sales distribution network.

Results

| (\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|-------|-------|
| Premiums & deposits | 45% | \$ 81 | \$ 56 |
| Gross revenues | 51 | 101 | 67 |
| Average assets | 67 | 500 | 300 |
| Number of: | | | |
| Career sales – agents | 22 | 554 | 455 |
| Assistance services – calls (thousands) | (3) | 681 | 699 |
| Policies under administration in the U.S. (thousands) | (6) | 4,100 | 4,342 |

RBC Investments

Business profile

RBC Investments provides full-service and self-directed brokerage, financial planning, investment counselling, personal trust, private banking and investment management products and services primarily to private clients in Canada, the U.S. and internationally. Products and services are delivered through the RBC Royal Bank branch network across Canada, RBC Investments offices, RBC Dain Rauscher branches in the U.S., private banking offices and other locations worldwide. Services are also delivered via the Internet and telephone. In September 2002, we realigned parts of our Canadian distribution channels under a single management structure to enhance the client experience by offering seamless, comprehensive solutions.

Industry profile

Wealth management is a highly competitive business with numerous large and boutique firms serving the affluent and high net worth client. Many of these firms have recently developed strategies focused on attracting the high net worth market. Volatile markets and the rising costs of managing the risks inherent in the business are changing the approach and profitability of some of the players. Consolidation in the mutual fund industry has not significantly altered the competitive landscape as distribution channels continue to be expanded by all players. Self-directed brokerage businesses have come under increased pressure due to reduced transaction volumes in light of market conditions, and clients using non-revenue generating services such as research, quotes and online asset mix calculators.

Our strengths

- Relationship management capabilities from experienced people and technology applications
- Ability to deliver the choice of products and services clients need to meet their financial goals
- Multiple distribution channels for client convenience
- Ability to access entire RBC client base
- Solutions designed for specific investment strategies and client risk tolerance

Our strategy

Our goal is to be a leading provider of personalized, comprehensive investment solutions for private clients worldwide, aligning them with client needs and the markets where we serve them.

In Canada:

- Match distribution channel and type of service to client needs and preferences
- Seek lifelong and intergenerational relationships with clients by offering products and services for each stage of their wealth management needs

In the United States:

- Grow through broadening and deepening relationships with existing clients as well as through targeted acquisitions over time in order to generate greater market share and scale

Internationally:

- Provide specialized global services to clients located around the world
- Offer solutions and provide advice and choice in an increasingly transparent international business

Outlook for 2003

Based on our expectation that investor confidence and capital markets performance will begin improving only by the third quarter of 2003, we expect moderate revenue growth in 2003. Cost containment efforts should help to keep the rate of expense growth below that of revenue growth. Retention compensation costs relating to recent U.S. acquisitions are forecast to be approximately \$40 million lower in 2003, further contributing to net income growth.

Financial performance

Net income was down 33% while core net income was up 44%. The growth in core net income was due to higher earnings from RBC Dain Rauscher, as well as the cessation of goodwill amortization this year (goodwill amortization was \$107 million in 2001). RBC Dain Rauscher's net income was \$3 million in 2002, compared to a loss of \$73 million last year (\$33 million loss excluding goodwill amortization). The improvement in RBC Dain Rauscher's net income occurred despite higher retention compensation costs and reflected the acquisition of Tucker Anthony Sutro on October 31, 2001 (since integrated into RBC Dain Rauscher) and strong performance from its fixed income division. Excluding RBC Dain Rauscher, core net income would have grown 9%, largely due to the cessation of goodwill amortization in 2002. ROE was largely unchanged from last year, excluding the gain on the sale of RT Capital Management.

Core ROE fell to 11.0% from 12.2%, due largely to an additional \$1.2 billion of average common equity attributed to the segment in 2002. Of the increase in average common equity, \$700 million related to goodwill arising from the acquisition of Tucker Anthony Sutro and most of the remainder to revised capital attribution for operational risk pertaining to this business segment.

Revenues were up 12% from 2001, or 26% excluding special items in 2001. Revenue growth reflected the acquisition of Tucker Anthony Sutro and strong results from the fixed income division of RBC Dain Rauscher. Excluding RBC Dain Rauscher's revenue growth of \$875 million, core revenues were down 6% due to weak client trading volumes in 2002.

Expenses increased 25% over a year ago, reflecting the acquisition of Tucker Anthony Sutro and higher retention compensation related to U.S. acquisitions, which increased to \$107 million from \$88 million in 2001, with \$45 million attributable to Tucker Anthony Sutro. RBC Dain Rauscher contributed \$774 million of the expense growth in 2002. Excluding RBC Dain Rauscher, expenses fell 9%, reflecting the cessation of goodwill amortization this year, higher expenses in 2001 from a \$38 million writedown of goodwill relating to Connor Clark, and good expense management.

Results

| (\$ millions, except percentage amounts) | % change | 2002 | 2001 |
|--|-----------|---------|---------|
| Net interest income | (4)% | \$ 371 | \$ 385 |
| Other income | 14 | 3,274 | 2,861 |
| Gross revenues | 12 | 3,645 | 3,246 |
| Provision for credit losses | | | |
| Allocated specific | (150) | (1) | 2 |
| Total | (150) | (1) | 2 |
| Non-interest expense (1) | 25 | 3,146 | 2,507 |
| Net income before income taxes | (32) | 500 | 737 |
| Income taxes | (30) | 157 | 224 |
| Net income | (33)% | \$ 343 | \$ 513 |
| U.S. net income | n.m. | \$ (2) | \$ (81) |
| Net income as a % of total bank net income | (900)bp | 12% | 21% |
| ROE | (1,620)bp | 11.0% | 27.2% |
| Economic Profit | (117)% | \$ (17) | \$ 101 |
| Average common equity | 67 | 3,000 | 1,800 |
| Core results (2) | | | |
| Gross revenues | 26 | 3,645 | 2,897 |
| Net income | 44 | 343 | 239 |
| ROE | (120)bp | 11.0% | 12.2% |
| Number of employees (full-time equivalent) | 14% | 12,001 | 10,512 |

(1) Includes goodwill amortization expense of \$107 million in 2001 (nil in 2002).
(2) Excluding special items in 2001 detailed in Table 6 on page 27A. Only the lines affected by special items are shown here.
n.m. not meaningful

Strategy by division

Canada

Financial Planning

The new financial planning platform is operated jointly with RBC Banking. This group serves branch-based clients typically with more than \$50,000 in investable assets of which a portion must include mutual funds or managed products. Financial planning has 1,100 relationship financial planners and 550 commission-based investment and retirement planners who are also financial planners and licensed mutual fund salespeople.

Canadian & International Brokerage group

This group includes our private client division (full-service brokerage) and RBC Action Direct (self-directed brokerage) and serves both investors requiring advisor-based comprehensive financial solutions and self-managed investors. Services are provided by over 1,420 investment advisors, over 180 investment representatives, as well as via telephone and the Internet. This group also includes the International Advisory Group, which has both Canadian and internationally-based employees serving international clients. Our goal is to maintain our market position in Canada by continuing to build and enhance existing client relationships.

RBC Global Private Banking (Canada)

Our private counsel, personal trust and private banking groups serve high net worth clients across Canada, and offer a relationship management approach for the client in need of sophisticated solutions. This group works with RBC Global Private Banking (international) to ensure we can serve clients who have interests in Canada as well as around the world. In Canada, 60 investment counsellors, 80 trust officers and 200 private bankers are in locations across the country.

Global Asset Management

This unit includes RBC Global Investment Management and RBC Funds, Canada's second largest mutual fund company. We directly manage more than \$40 billion of assets in mutual and pooled funds as well as other client assets. We provide proprietary and externally-managed investment management products and advisory services through RBC Royal Bank, RBC Investments' distribution businesses and external distributors to private and institutional clients in Canada and worldwide. Our family of mutual funds and other pooled products encompass a broad range of investment solutions including money market, fixed income, balanced and Canadian, U.S. and global equity funds, as well as alternative investments. In 2003, our goal is to continue the strategy, first implemented in 2001, to broaden the distribution channels for investment management services and mutual fund products. This strategy has contributed to a 12% increase in our share of the Canadian mutual fund market over the past two years.

United States

RBC Dain Rauscher

Minneapolis-based RBC Dain Rauscher comprises a full-service brokerage subsidiary and a fixed income business. RBC Dain Rauscher plans to grow through broadening and deepening relationships with existing clients by understanding their needs and the potential profitability of the client relationship. We also plan to grow by focusing on opportunities which generate greater market share and scale within our existing markets. The integration of Boston-based Tucker Anthony Sutro was completed in 2002 and made RBC Dain Rauscher the 9th-largest full-service securities firm in the U.S., with close to 2,000 financial consultants serving individual clients from coast to coast and a fixed income business with 280 investment bankers, sales representatives and traders serving institutional and retail clients nationwide.

International

RBC Global Private Banking

This internationally-focused unit provides private banking, trust and investment counselling solutions to high net worth clients in more than 100 countries. Our goal is to provide specialized global services to high net worth clients with assets of more than \$1 million. In 2003, we intend to grow revenues by leveraging CRM capabilities within the group, by exploring potential European and North and South American acquisitions, and by building alliances in markets where we already have a presence. The addition of non-proprietary money management capabilities will expand our value proposition to clients.

Financial highlights by division

RBC Investments' revenues grew 12% from last year for the reasons mentioned on page 32A. The decline in revenues from the Canadian & International Brokerage group was due to lower transaction- and fee-based revenues, reflecting continued weakness in capital markets. Global Asset Management's revenues declined 57% as revenues in 2001 included a \$313 million gain on the sale of RT Capital Management and 10 months of results from that business that did not recur in 2002.

Revenues

| (\$ millions) | % change | 2002 | 2001 |
|------------------------------------|----------|----------|----------|
| Canadian & International Brokerage | (9)% | \$ 984 | \$ 1,076 |
| RBC Dain Rauscher (1) | 106 | 1,702 | 827 |
| RBC Global Private Banking (2) | 5 | 678 | 643 |
| Global Asset Management (3) | (57) | 286 | 660 |
| Other (4) | (112) | (5) | 40 |
| | 12% | \$ 3,645 | \$ 3,246 |

- (1) 2002 revenues include Tucker Anthony Sutro acquired on October 31, 2001.
 (2) Includes both Canadian and international businesses and Financial Planning.
 (3) 2001 revenues included RT Capital Management until August 15, 2001 and a \$313 million gain on the sale of RT Capital Management.
 (4) 2001 revenues included a \$36 million gain on the sale of Group Retirement Services. Excluding this gain, 2001 revenues were \$4 million.

Despite difficult capital market conditions, our Canadian & International Brokerage group was able to grow its assets, with much of the growth coming from fee-generating assets. Higher AUA in RBC Global Private Banking were related to an increase in new business, the acquisition of the assets of Barclays Bank PLC's private banking operations in the Americas and a 5% increase in the value of the British pound against the Canadian dollar. These increases largely offset lower AUA at RBC Dain Rauscher, due to declines in market values, as well as an expected decrease related to broker attrition resulting from weak market conditions and the integration of Tucker Anthony Sutro into RBC Dain Rauscher.

Assets under administration

| (\$ millions) | % change | 2002 | 2001 |
|------------------------------------|----------|-----------|------------|
| Personal | | | |
| Canadian & International Brokerage | 3% | \$111,340 | \$ 107,760 |
| RBC Dain Rauscher | (18) | 132,930 | 161,740 |
| RBC Global Private Banking | 21 | 82,390 | 67,990 |
| | (3) | 326,660 | 337,490 |
| Institutional | | | |
| RBC Global Private Banking | 14 | 69,730 | 61,010 |
| | (1)% | \$396,390 | \$ 398,500 |

The decline in personal AUM largely reflected lower asset values due to weak capital market conditions. As part of the integration of Tucker Anthony Sutro into RBC Dain Rauscher, a non-core asset management business which was acquired as part of Tucker Anthony Sutro was divested, contributing to the decrease in personal AUM. Much of the increase in institutional AUM was related to the accumulation of new assets in RBC Global Private Banking and at RBC Dain Rauscher. Mutual fund asset levels remained relatively stable with lower market values offset by strong net sales driven by a successful RRSP campaign.

Assets under management

| (\$ millions) | % change | 2002 | 2001 |
|---------------|----------|-----------|-----------|
| Personal | (23)% | \$ 35,660 | \$ 46,620 |
| Institutional | 9 | 18,410 | 16,940 |
| Mutual funds | (1) | 34,230 | 34,550 |
| | (10)% | \$ 88,300 | \$ 98,110 |

RBC Capital Markets

Business profile

RBC Capital Markets provides wholesale financial services to large corporate, government and institutional clients in North America and in specialized product and industry sectors globally. Headquartered in Toronto, RBC Capital Markets has key centres of expertise in Minneapolis, New York and London, and offices in 27 other cities.

Industry profile

The Canadian wholesale financial services market is mature and, as a result, many Canadian firms are seeking growth opportunities outside of their domestic market, primarily in the U.S. The U.S. capital markets are dominated by several large global investment banks whose principal focus is on the top tier of companies forming the S&P 500. However, we believe significant opportunities exist for specialized players targeting the lower end of the S&P 500. To succeed in the North American context requires the ability to provide clients with innovative, value-added solutions that reflect a keen understanding of both the company and industry sector. Increasingly, new business opportunities will accrue to those firms with a reputation for adhering to high ethical standards.

Our strengths

- Top-tier market shares in virtually all lines of business in Canada
- Established reputation as a premier Canadian investment dealer as evidenced by our market share leadership
- Superior origination and distribution capability as measured by our standings in underwriting league tables
- Expertise and market knowledge in a broad array of industries

Our strategy

Our goals are to be recognized as the leading corporate and investment bank in Canada based on external rankings and to build a successful integrated North American business, while continuing to expand our specialized global businesses.

Key strategies for RBC Capital Markets include the following:

- In Canada, to maintain our position as a leading full-service provider in all of our markets by continuing to leverage the breadth of our long-standing client relationships, the depth of our trading, research and sales capabilities, and the strength of our brand and reputation in the Canadian market
- In the U.S., to provide value-added solutions by offering clients a broad product portfolio delivered through specialized industry teams, with the goal of building an integrated North American franchise. We will leverage the depth of our research and advisory capabilities in targeted North American industry sectors, specifically energy, technology, communications, health care, consumer products, and mid-size financial institutions
- Continue to expand our global specialized businesses by providing clients with customized, value-added solutions in the areas of bonds, money markets, foreign exchange, structured finance and equity and credit derivatives

Outlook for 2003

Given our expectations for reasonable economic growth in both Canada and the U.S. and a moderate capital markets recovery in 2003, we are anticipating modest revenue growth in 2003. Our outlook is based on the expectation of a recovery in trading volumes, merger and acquisition activities and new issue and advisory mandates to more normalized levels. We intend to maintain our focus on strategic cost management and to keep the rate of expense growth below that of revenue growth. We also plan to continue to proactively manage the credit risk associated with our corporate loan portfolio.

Financial performance

Net income increased 24%, or 15% on a core basis, as expenses fell far more than did revenues. Core ROE was virtually unchanged from 2001, with higher net income offset by \$700 million of additional common equity attributed to the segment compared to last year, reflecting a change in methodology for attributing capital relating to credit risk.

Revenues declined \$111 million or 4% from last year, due largely to lower trading revenues in our platform resulting from continued weakness in capital markets and lower lending revenues due to targeted reductions in the corporate loan portfolio.

Non-interest expense fell \$177 million or 10% due to a lower number of employees and reduced variable compensation costs. Retention compensation costs related to the acquisition of Dain Rauscher Wessels, fully integrated into RBC Capital Markets since early 2002, were also lower, falling to \$51 million from \$88 million in 2001.

The provision for credit losses increased by \$58 million or 14% from 2001, due primarily to certain telecommunication, cable and energy accounts that were classified as impaired during the year. The increase in the provision for credit losses was partially offset by related credit derivative gains which were recorded in other income. Net impaired loans were down \$22 million or 5% from last year, reflecting write-offs in the corporate loan portfolio.

The decline in income taxes was attributable to tax rate differentials in various jurisdictions, as well as higher income taxes in 2001 resulting from a special \$28 million income tax expense shown in Table 6 on page 27A.

Results

| (\$ millions, taxable equivalent basis, except percentage amounts) | % change | 2002 | 2001 |
|---|----------|---------|---------|
| Net interest income | 29% | \$ 553 | \$ 430 |
| Other income | (10) | 2,112 | 2,346 |
| Gross revenues | (4) | 2,665 | 2,776 |
| Provision for credit losses | | | |
| Allocated specific | 14 | 465 | 407 |
| Total | 14 | 465 | 407 |
| Non-interest expense (1) | (10) | 1,627 | 1,804 |
| Net income before income taxes | 1 | 573 | 565 |
| Income taxes | (35) | 135 | 208 |
| Taxable equivalent adjustment | — | 21 | 21 |
| Net income | 24% | \$ 417 | \$ 336 |
| U.S. net income | n.m. | \$ (40) | \$ (77) |
| Net income as a % of total bank net income | 100 bp | 15% | 14% |
| ROE | 70 bp | 10.0% | 9.3% |
| Economic Profit | n.m. | \$ (76) | \$ (56) |
| Average assets | 14% | 178,200 | 156,400 |
| Average loans, acceptances and reverse repurchase agreements | 3 | 61,400 | 59,600 |
| Average deposits | 12 | 79,200 | 70,500 |
| Average common equity | 21 | 4,000 | 3,300 |
| Core results (2) | | | |
| Net income | 15 | 417 | 364 |
| ROE | (10)bp | 10.0% | 10.1% |
| Credit information | | | |
| Net impaired loans | (5)% | \$ 390 | \$ 412 |
| Net write-offs | 120 | 510 | 232 |
| Net write-offs as a % of average loans, acceptances and reverse repurchase agreements | 44 bp | .83% | .39% |
| Number of employees (full-time equivalent) | (1)% | 2,938 | 2,954 |

(1) Includes goodwill amortization expense of \$43 million in 2001 (nil in 2002).

(2) Excluding special items in 2001 detailed in Table 6 on page 27A. Only the lines affected by special items are shown here.

n.m. not meaningful

Strategy by division

Capital Markets Services

This division was formed in November 2001, combining the equity research, sales and trading businesses with the corporate and investment banking businesses. We offer a full range of credit and corporate finance products, including debt and equity underwriting, mergers & acquisitions (M&A) advice and execution, and expertise in research and equity sales and trading activities.

In Canada, we will build on our key strengths – expert knowledge of the Canadian markets, breadth and longevity of client relationships, depth in trading, research and sales and a long-standing reputation as a top-ranked domestic investment bank – to continue to be a full-service provider to all industries.

On a North American basis, we will be industry-focused – specifically technology, telecommunication, health care, energy, consumer products and mid-size financial institutions. By leveraging our research and advisory capabilities, we expect to differentiate ourselves on our ability to provide superior knowledge of investment opportunities and market-based solutions for our target clients.

Global Financial Products

This division was formed in November 2001 to address the continuing convergence of financial products available to clients. Its formation brought together the business activities involving the origination, syndication, securitization, trading and distribution of debt products globally. These products include loans, bonds and derivatives at both the investment grade and sub-investment grade levels. As well, Global Financial Products provides leveraged product asset management capabilities and is the centre of expertise for RBC Capital Markets' proprietary trading activities. The combination of these businesses provides the ability to maximize internal expertise and deliver a broad array of value-added ideas and solutions to clients.

We intend to continue to focus on identifying opportunities where we can build from our existing strengths to provide solutions-based approaches to structuring transactions for our clients.

Global Treasury Services

Global Treasury Services combines our money markets and foreign exchange businesses and provides global clients with foreign exchange, commodities, derivatives and interest rate products, as well as currency risk management and advisory services. These products and services are delivered through our extensive global sales and trading network, operating from centres that include Toronto, London and New York. Recognized as a market leader in foreign exchange e-commerce solutions, we also deliver services through our Internet trading platform, FX Direct, and are a member of the multi-bank global trading platform, FXall. We will continue to invest in innovative electronic delivery channels that offer sophisticated and flexible products and services.

Global Credit

Global Credit provides centralized management of all credit exposure associated with our loan portfolio. While wholesale lending is fundamental to the attraction and expansion of high-margin client businesses, lending must be strategic in order to maximize the returns to shareholders. Our portfolio and transaction management specialists use sophisticated risk management and analytical tools designed to ensure that the pricing on loans is commensurate with the associated risk and reflects the value of all products and services a client has with RBC.

Our transaction specialists use appropriate structures to provide clients with value-added, as opposed to commoditized, credit solutions. We work closely with our distribution teams to further reduce the size of our corporate lending base, while continuing to enhance the quality of earnings from this source.

Alternative investments

Alternative Investments was formed in June 2002 with a mandate to expand our wholesale asset management capabilities, which today include operations in hedge funds and private equity. The alternative asset business provides non-traditional investment opportunities to high net worth individuals, corporations and institutional clients. These investment options include private equity and hedge funds, and can extend to other vehicles such as leveraged buyouts, Collateralized Debt Obligations (CDOs) and managed futures. We are uniquely positioned to leverage our existing infrastructure and our superior product knowledge across other businesses within RBC who have strong relationships with our target client base.

Financial highlights by division

Revenues were up 3% from 2001. Factors contributing to this increase include strong performance in Canadian equity new issue and M&A business and credit derivative gains related to accounts that were classified as impaired during the year. These factors offset lower sales and trading revenues, weak performance in U.S. equity new issue and M&A business and a 9% decline in core lending revenues. Core lending revenues decreased due to tightened spreads and the targeted reduction in the corporate loan portfolio, which is also reflected in the 13% decline in average assets.

Results

| (\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|----------|----------|
| Gross revenues | 3% | \$ 1,063 | \$ 1,034 |
| Average assets | (13) | 13,600 | 15,700 |

Revenues were up 5% in 2002. Favourable interest rate trading environments during the year helped to fuel revenue and asset growth from our traditional bond and derivative businesses, as well as revenue growth from new initiatives developed in securitization, leveraged finance and asset management. Revenues from our proprietary trading activities were down slightly from 2001 levels. Overall, this business achieved strong performance despite difficult markets and business limitations resulting from the displacement of our New York operations after the events of September 11th.

Results

| (\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|--------|--------|
| Gross revenues | 5% | \$ 884 | \$ 839 |
| Average assets | 41 | 70,700 | 50,200 |

Revenues were down 18% from 2001, which was a record year. The foreign exchange businesses experienced increased volatility in foreign exchange rates and decreased volumes, while economic and interest rate uncertainty negatively affected the money markets businesses. However, the derivative-based businesses performed well and we continued to grow revenues through e-commerce channels.

Results

| (\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|--------|--------|
| Gross revenues | (18)% | \$ 510 | \$ 619 |
| Average assets | 6 | 76,000 | 72,000 |

Global Credit's 45% decline in revenues was mainly driven by net negative mark-to-market adjustments on credit derivatives and other financial instruments and targeted reductions in our non-core lending portfolio, which is reflected in the 25% decline in average assets. These decreases offset revenue growth from our structured lending business and our successful efforts to transition towards higher-value loan transactions with greater liquidity.

Results

| (\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|--------|--------|
| Gross revenues | (45)% | \$ 112 | \$ 203 |
| Average assets | (25) | 10,100 | 13,500 |

Revenues were up 19%, with strong results from our hedge fund business, which accounts for the majority of our revenues, and stable results from proprietary trading offsetting lower revenues from the Canadian equity derivatives business. Revenues from our merchant banking business were also lower due to lower capital gains and the writedowns of certain investments.

Results

| (\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|-------|-------|
| Gross revenues | 19% | \$ 96 | \$ 81 |
| Average assets | 56 | 7,800 | 5,000 |

RBC Global Services

Business profile

RBC Global Services offers specialized transaction processing services to business, commercial, corporate and institutional clients in domestic and select international markets. Key businesses include investment administration, correspondent banking, cash management, payments and trade finance. Our 50% interest in the Moneris Solutions merchant card processing joint venture is reported under RBC Global Services.

Industry profile

The industry is characterized by increasing consolidation as certain segments become more global. Monoline specialists and new market entrants compete against traditional financial institutions. Scale is increasingly important to support the significant investment in technology required to introduce new products and services, accommodate industry-driven infrastructure changes and enhance operational efficiencies.

Our strengths

- We have a leadership position in Canada in these businesses as measured by AUA and market share of number of client relationships
- We have strong client relationships as evidenced by our high rate of client retention and new business generated from existing clients
- We are recognized for quality of service as evidenced by our top rankings in third-party client surveys
- We continue to develop and deploy new technology and client service solutions
- We are able to leverage our market position by aligning the resources within RBC Global Services with the expertise of other RBC platforms to offer a superior integrated service to the market

Our strategy

Our goal is to maintain and enhance our leadership position in Canada while continuing to develop a competitive international presence. To meet our goal, we will:

- Build upon existing client relationships to develop new business in select domestic and international markets
- Grow the business through key alliances, acquisitions and partnerships and continue to leverage the Moneris Solutions joint venture
- Drive revenue growth by developing new products and selling higher-margin value-added services, such as securities lending and trade advisory
- Enhance our processing and systems platforms to deliver new capabilities, improve efficiencies and drive economies of scale
- Continue the shift to electronic payment products and services focusing on Web-based solutions.

Outlook for 2003

Although we expect interest rates to rise in the second half of 2003, they will likely remain low in historical terms, which will continue to have an unfavourable impact on our revenue growth in 2003. As our revenues earned on deposits and cash balances are highly dependent upon the interest rate environment, our net interest income growth may be adversely affected. At the same time, the expectation of a modest recovery in capital markets beginning in the second half of 2003 should have a favourable impact on revenues from foreign exchange and on fee revenues from higher AUA.

Financial performance

Net income declined 35% while core net income, excluding the gain on the formation of the Moneris Solutions joint venture in 2001, declined 8% from last year, partially reflecting an increase in the provision for credit losses.

ROE was 28.4% compared to core ROE of 34.3% in 2001. The decline in ROE reflects lower net income as well as a \$100 million increase in average common equity attributed to this segment in 2002. The higher common equity reflects the 50% interest in the Moneris Solutions joint venture and higher capital attribution for operating risk.

Revenues were down 4% from last year, reflecting lower interest income due to the low interest rate environment, as well as lower foreign exchange revenues, which more than offset a 10% increase in fee income. Core revenues (which exclude an \$89 million gain on the formation of the Moneris Solutions joint venture) were up 5%. Revenues were positively affected by the acquisition of Perpetual Fund Services (an Australian custody, investment administration and unit registry business) on July 31, 2001 and a change pertaining to the classification of services provided by us to Moneris Solutions, effective November 2001. Payments for services provided to Moneris Solutions are now being treated as revenues, whereas previously they were treated as cost recoveries. Excluding these factors, revenues were flat.

Expenses were \$69 million or 12% higher in 2002 due to the inclusion of a full year of Perpetual Fund Services as well as continued investments in technology. Excluding the acquisition of Perpetual Fund Services and the change in the classification of services provided by us to Moneris Solutions discussed above, expenses increased by 5%.

The increases in both the provision for credit losses and net impaired loans were associated with Argentine loans classified as impaired during the year.

Results

| (\$ millions, except percentage amounts) | % change | 2002 | 2001 |
|--|-----------|--------|---------|
| Net interest income | (7)% | \$ 137 | \$ 147 |
| Other income | (4) | 820 | 851 |
| Gross revenues | (4) | 957 | 998 |
| Provision for credit losses | | | |
| Allocated specific | n.m. | 10 | (2) |
| Total | n.m. | 10 | (2) |
| Non-interest expense (1) | 12 | 668 | 599 |
| Net income before income taxes | (30) | 279 | 401 |
| Income taxes | (22) | 108 | 138 |
| Net income | (35)% | \$ 171 | \$ 263 |
| U.S. net income | (41) | \$ 10 | \$ 17 |
| Net income as a % of total bank net income | (500)bp | 6% | 11% |
| ROE | (2,050)bp | 28.4% | 48.9% |
| Economic Profit | (19)% | \$ 98 | \$ 121 |
| Average common equity | 20 | 600 | 500 |
| Core results (2) | | | |
| Gross revenues | 5 | 957 | 909 |
| Net income | (8) | 171 | 186 |
| ROE | (590)bp | 28.4% | 34.3% |
| Credit information | | | |
| Net impaired loans | n.m. | \$ — | \$ (11) |
| Net write-offs | (114)% | (1) | 7 |
| Net write-offs as a % of average loans and acceptances | (40)bp | (.05)% | .35% |
| Number of employees | | | |
| (full-time equivalent) | 1% | 2,571 | 2,557 |

(1) Includes goodwill amortization expense of \$8 million in 2001 (nil in 2002).

(2) Excluding special items in 2001 detailed in Table 6 on page 27A. Only the lines affected by special items are shown here.

n.m. not meaningful

Strategy by division

Institutional & Investor Services

Institutional & Investor Services is Canada's largest custodian as measured by AUA, and a leading provider of investment administration services to corporate and institutional investors worldwide. We operate from 13 locations throughout the world, with a global custody network spanning 80 markets.

We plan to continue to leverage our leadership position in the Canadian market to expand internationally, with a focus on serving fund managers, financial institutions and private banks.

We expect to achieve growth in our fee-based revenue streams by:

- Selling newly developed products and services to existing clients
- Expanding our client offerings in Europe and Asia-Pacific
- Further exploring alliance and acquisition opportunities

Financial Institutions

A comprehensive range of correspondent banking services is provided to banks globally and to broker-dealers within Canada, including cash management, payments, clearing, trade, foreign exchange, derivatives lending, securities lending, custody and settlement, and structured financing.

Our goal is to leverage our leadership position in the Canadian dollar clearing market and our client relationships by:

- Identifying differentiated value-added solutions that address the unique needs of the different market segments
- Adding new revenue streams by introducing service offerings that integrate the new product developments of RBC Global Services with those of other business platforms

We will continue to monitor and actively manage our exposure to higher risk markets.

Treasury Management & Trade

Treasury Management & Trade provides cash management, payment and trade services to business, commercial, corporate and public sector segments. Our trade team provides Canadian and foreign importers and exporters with a variety of trade products, services and counsel. Our cash management group provides a range of solutions to clients that allow for more effective cash flow and integration with client processing. Through Moneris Solutions we provide merchants with credit and debit card transaction processing services.

Our goal is to continue to be the leading provider in Canada by retaining profitable client relationships and growing market share in strategic markets by:

- Introducing a market segmentation approach that accommodates the diverse needs of business markets
- Expanding the functionality of our Web-based delivery channel for both cash management and trade services
- Introducing new trade products and services as well as expanding trade alliances to meet clients' international trade requirements while effectively managing risk
- Leveraging our cash management sales and service leadership position

Financial highlights by division

Revenues grew \$3 million or 1% in 2002, as the positive impact of the Perpetual Fund Services acquisition and higher fee income offset lower revenues from foreign exchange and interest income, due to the low interest rate environment. AUA increased by 3% from 2001 due to new business, but the effect of equity market declines largely offset the additions.

Results

| (\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|---------|---------|
| Gross revenues | 1% | \$ 401 | \$ 398 |
| Assets under administration | 3 | 963,200 | 936,700 |

Revenues fell \$15 million or 13% from last year, primarily due to a decrease in interest income associated with the low interest environment. In addition, certain fee revenues were transferred from RBC Global Services to RBC Capital Markets in 2002, contributing to the decline in revenues. The decrease in average assets reflected strategic reductions in the size of our Latin American loan portfolio, which now totals \$146 million.

Results

| (\$ millions, taxable equivalent basis) | % change | 2002 | 2001 |
|---|----------|-------|--------|
| Gross revenues | (13)% | \$ 98 | \$ 113 |
| Average assets | (15) | 1,700 | 2,000 |
| Average deposits | — | 1,700 | 1,700 |

Revenues decreased \$29 million or 6% from 2001. Excluding the \$89 million gain on the formation of the Moneris Solutions joint venture in 2001, revenues increased \$60 million or 15%. This increase primarily reflected a change pertaining to the classification of services provided by us to Moneris Solutions, effective November 2001. Payment for services provided to Moneris Solutions are now being treated as revenues, whereas previously they were treated as cost recoveries. Excluding this factor, revenues increased 10%, reflecting growth in fee income.

Results

| (\$ millions, taxable equivalent basis, volumes in thousands) | % change | 2002 | 2001 |
|---|----------|--------|--------|
| Gross revenues | (6)% | \$ 458 | \$ 487 |
| Core gross revenues (1) | 15 | 458 | 398 |
| Average deposits | 6 | 6,350 | 6,000 |
| Payment volumes (2) | 12 | 7,440 | 6,670 |
| Payment errors (per 10,000 payments) | (40) | .33 | .55 |

(1) Excluding special items in 2001 detailed in Table 6 on page 27A.

(2) Restated to include payment types not previously included in 2001.

Financial priority: Revenue growth and diversification

Highlights

- Revenues up 7%
- Operating (core) revenues up 10%, reflecting acquisitions
- Excluding recent U.S. acquisitions, operating revenues were unchanged
- Net interest income up 10%
- Net interest margin of 1.96%, down four basis points
- Other income up 4% and core other income up 10%
- Other income 54% of total revenues

TABLE 7 Operating revenues

| (\$ millions, taxable equivalent basis) | 2002 | 2001 | 2002 vs 2001 Increase (decrease) | |
|--|-----------|-----------|-------------------------------------|------|
| Net interest income | \$ 7,198 | \$ 6,549 | \$ 649 | 10% |
| Other income | 8,562 | 8,215 | 347 | 4 |
| Total revenues (reported) | 15,760 | 14,764 | 996 | 7 |
| Less: Special items (1) | — | (445) | (445) | n.m. |
| Operating revenues | 15,760 | 14,319 | 1,441 | 10 |
| Less: Revenues of recent U.S. acquisitions (2) | (3,190) | (1,687) | 1,503 | 89 |
| Operating revenues, excluding recent U.S. acquisitions | \$ 12,570 | \$ 12,632 | \$ (62) | —% |

(1) Special items in 2001 are described in Table 6 on page 27A. There were no special items for 2002.

(2) Represents revenues of RBC Centura (now includes Eagle Bancshares, RBC Mortgage for the purposes of this discussion and analysis and what was previously SFNB), RBC Liberty Insurance and RBC Dain Rauscher (includes Tucker Anthony Sutro) and excludes Dain Rauscher Wessels, which was integrated into RBC Capital Markets in early 2002.

n.m. not meaningful.

Total revenues were up \$1.0 billion or 7% from 2001. Operating, or core, revenues (which exclude \$445 million of gains from special items recorded in 2001) were up \$1.4 billion or 10% from a year ago.

As shown in the table above, revenues from recent U.S. acquisitions accounted for all of the growth in operating revenue. Excluding recent U.S. acquisitions, operating revenues were unchanged from a year ago. This compared to a decline in operating expenses of 5% (discussed in the Cost control section on page 42A).

Net interest income

Net interest income was up 10% from 2001 to \$7.2 billion. The majority of the increase stemmed from recent U.S. acquisitions. If these acquisitions are excluded, net interest income would have been up 2% due to an increase in the amount of interest-earning assets, particularly residential mortgages, which more than offset a narrower spread on deposits.

As shown in Table 8 below, the net interest margin decreased by four basis points from last year to 1.96%, reflecting a narrower spread between the prime rate and core deposit funding costs resulting from a reduction in the average Canadian prime rate to 4.15% from 6.55% in 2001.

TABLE 8 Net interest income and margin

| (\$ millions, except percentage amounts) | 2002 | 2001 | 2000 |
|--|------------|------------|------------|
| Average assets | \$ 367,300 | \$ 327,100 | \$ 281,900 |
| Net interest income (1) | 7,198 | 6,549 | 5,307 |
| Net interest margin (2) | 1.96% | 2.00% | 1.88% |

(1) Taxable equivalent basis.

(2) Net interest income, on a taxable equivalent basis, as a percentage of average assets.

Outlook

We are targeting core revenue growth of 5–8% in fiscal 2003, based on our expectations that capital market activity will pick up somewhat, interest rates in Canada will rise and the Canadian and U.S. economies will grow somewhat faster than in 2002.

TABLE 9 Net interest income on average assets and liabilities

| (\$ millions, taxable equivalent basis, except percentage amounts) | Average balances (1) | | | Interest (2) | | | Average rate | | |
|--|----------------------|------------|------------|--------------|-----------|-----------|--------------|-------|-------|
| | 2002 | 2001 | 2000 | 2002 | 2001 | 2000 | 2002 | 2001 | 2000 |
| Assets | | | | | | | | | |
| Deposits with banks | | | | | | | | | |
| Canada | \$ 367 | \$ 449 | \$ 612 | \$ 7 | \$ 18 | \$ 22 | 1.91% | 4.01% | 3.59% |
| International | 15,382 | 16,154 | 13,888 | 476 | 813 | 802 | 3.09 | 5.03 | 5.77 |
| | 15,749 | 16,603 | 14,500 | 483 | 831 | 824 | 3.07 | 5.01 | 5.68 |
| Securities | | | | | | | | | |
| Trading account | 65,422 | 51,429 | 38,450 | 1,945 | 2,143 | 1,519 | 2.97 | 4.17 | 3.95 |
| Investment account | 25,171 | 21,154 | 20,142 | 1,127 | 1,125 | 1,129 | 4.48 | 5.32 | 5.61 |
| Loan substitute | 407 | 463 | 495 | 43 | 45 | 49 | 10.57 | 9.72 | 9.90 |
| | 91,000 | 73,046 | 59,087 | 3,115 | 3,313 | 2,697 | 3.42 | 4.54 | 4.56 |
| Assets purchased under reverse repurchase agreements | 35,463 | 29,591 | 21,729 | 651 | 1,163 | 1,078 | 1.84 | 3.93 | 4.96 |
| Loans (3) | | | | | | | | | |
| Canada | | | | | | | | | |
| Residential mortgage | 65,901 | 62,448 | 59,860 | 3,903 | 4,087 | 3,891 | 5.92 | 6.54 | 6.50 |
| Personal | 26,631 | 28,089 | 26,949 | 1,734 | 2,325 | 2,290 | 6.51 | 8.28 | 8.50 |
| Credit card | 4,354 | 4,586 | 3,559 | 519 | 556 | 405 | 11.92 | 12.12 | 11.38 |
| Business and government | 28,650 | 32,347 | 32,927 | 1,291 | 1,281 | 1,506 | 4.51 | 3.96 | 4.57 |
| | 125,536 | 127,470 | 123,295 | 7,447 | 8,249 | 8,092 | 5.93 | 6.47 | 6.56 |
| International | 41,132 | 32,836 | 24,495 | 3,016 | 3,783 | 3,446 | 7.33 | 11.52 | 14.07 |
| | 166,668 | 160,306 | 147,790 | 10,463 | 12,032 | 11,538 | 6.28 | 7.51 | 7.81 |
| Total interest-earning assets | 308,880 | 279,546 | 243,106 | 14,712 | 17,339 | 16,137 | 4.76 | 6.20 | 6.64 |
| Non-interest-bearing deposits with banks | 1,753 | 1,188 | 930 | | | | | | |
| Customers' liability under acceptances | 8,515 | 9,890 | 10,281 | | | | | | |
| Other assets | 48,152 | 36,476 | 27,583 | | | | | | |
| Total assets | \$ 367,300 | \$ 327,100 | \$ 281,900 | \$ 14,712 | \$ 17,339 | \$ 16,137 | 4.01% | 5.30% | 5.72% |
| Liabilities and shareholders' equity | | | | | | | | | |
| Deposits (4) | | | | | | | | | |
| Canada | \$ 111,880 | \$ 110,228 | \$ 107,533 | \$ 2,964 | \$ 4,712 | \$ 5,060 | 2.65% | 4.27% | 4.71% |
| International | 108,620 | 89,629 | 70,575 | 2,745 | 4,000 | 3,997 | 2.53 | 4.46 | 5.66 |
| | 220,500 | 199,857 | 178,108 | 5,709 | 8,712 | 9,057 | 2.59 | 4.36 | 5.09 |
| Obligations related to securities sold short | 19,912 | 16,509 | 14,195 | 797 | 654 | 656 | 4.00 | 3.96 | 4.62 |
| Obligations related to assets sold under repurchase agreements | 19,630 | 19,892 | 11,873 | 414 | 894 | 653 | 2.11 | 4.49 | 5.50 |
| Subordinated debentures | 6,804 | 6,805 | 5,129 | 406 | 410 | 344 | 5.97 | 6.02 | 6.71 |
| Other interest-bearing liabilities | 5,546 | 3,042 | 3,042 | 188 | 120 | 120 | 3.39 | 3.94 | 3.94 |
| Total interest-bearing liabilities | 272,392 | 246,105 | 212,347 | 7,514 | 10,790 | 10,830 | 2.76 | 4.38 | 5.10 |
| Non-interest-bearing deposits | 19,897 | 18,568 | 15,654 | | | | | | |
| Acceptances | 8,515 | 9,890 | 10,281 | | | | | | |
| Other liabilities | 47,974 | 36,621 | 30,829 | | | | | | |
| | 348,778 | 311,184 | 269,111 | 7,514 | 10,790 | 10,830 | 2.15 | 3.47 | 4.02 |
| Shareholders' equity | | | | | | | | | |
| Preferred | 1,713 | 2,073 | 1,975 | | | | | | |
| Common | 16,809 | 13,843 | 10,814 | | | | | | |
| Total liabilities and shareholders' equity | \$ 367,300 | \$ 327,100 | \$ 281,900 | \$ 7,514 | \$ 10,790 | \$ 10,830 | 2.05% | 3.30% | 3.84% |
| Net interest income as a % of total average assets | \$ 367,300 | \$ 327,100 | \$ 281,900 | \$ 7,198 | \$ 6,549 | \$ 5,307 | 1.96% | 2.00% | 1.88% |
| Net interest income as a % of total average interest-earning assets | | | | | | | | | |
| Canada | \$ 196,321 | \$ 182,904 | \$ 176,865 | \$ 6,539 | \$ 5,343 | \$ 4,796 | 3.33% | 2.92% | 2.71% |
| International | 112,559 | 96,642 | 66,241 | 659 | 1,206 | 511 | .59 | 1.25 | .77 |
| Total | \$ 308,880 | \$ 279,546 | \$ 243,106 | \$ 7,198 | \$ 6,549 | \$ 5,307 | 2.33% | 2.34% | 2.18% |

(1) Calculated on a daily basis.

(2) Interest income includes loan fees of \$321 million (2001 – \$328 million; 2000 – \$274 million). The taxable equivalent adjustment is based on the Canadian tax rate of 38.5% (2001 – 41.5%; 2000 – 42.8%) and U.S. federal tax rate of 39.5%.

(3) Average balances include impaired loans and are net of the allowance for credit losses.

(4) Deposits include savings deposits with average balances of \$39 billion (2001 – \$38 billion; 2000 – \$34 billion), interest expense of \$.3 billion (2001 – \$.6 billion; 2000 – \$.7 billion) and average rates of .69% (2001 – 1.58%; 2000 – 2.06%). Deposits also include time deposits with average balances of \$47 billion (2001 – \$44 billion; 2000 – \$38 billion), interest expense of \$1.3 billion (2001 – \$2.0 billion; 2000 – \$2.0 billion) and average rates of 2.86% (2001 – 4.55%; 2000 – 5.26%).

TABLE 10 Change in net interest income

| (\$ millions, taxable equivalent basis) | 2002 vs 2001 Increase (decrease) due to changes in | | | 2001 vs 2000 Increase (decrease) due to changes in | | |
|---|--|---------------------|-------------------|--|---------------------|-----------------|
| | average volume (1) | average rate (1) | Net change | average volume (1) | average rate (1) | Net change |
| Assets | | | | | | |
| Deposits with banks | | | | | | |
| Canada | \$ (3) | \$ (8) | \$ (11) | \$ (6) | \$ 2 | \$ (4) |
| International | (37) | (300) | (337) | 121 | (110) | 11 |
| Securities | | | | | | |
| Trading account | 502 | (700) | (198) | 537 | 87 | 624 |
| Investment account | 195 | (193) | 2 | 55 | (59) | (4) |
| Loan substitute | (6) | 4 | (2) | (3) | (1) | (4) |
| Assets purchased under reverse repurchase agreements | 197 | (709) | (512) | 339 | (254) | 85 |
| Loans | | | | | | |
| Canada | | | | | | |
| Residential mortgage | 218 | (402) | (184) | 169 | 27 | 196 |
| Personal | (116) | (475) | (591) | 95 | (60) | 35 |
| Credit card | (28) | (9) | (37) | 123 | 28 | 151 |
| Business and government | (156) | 166 | 10 | (26) | (199) | (225) |
| International | 813 | (1,580) | (767) | 1,035 | (698) | 337 |
| Total interest income | \$ 1,579 | \$ (4,206) | \$ (2,627) | \$ 2,439 | \$ (1,237) | \$ 1,202 |
| Liabilities | | | | | | |
| Deposits | | | | | | |
| Canada | \$ 70 | \$ (1,818) | \$ (1,748) | \$ 124 | \$ (472) | \$ (348) |
| International | 727 | (1,982) | (1,255) | 951 | (948) | 3 |
| Obligations related to securities sold short | 136 | 7 | 143 | 99 | (101) | (2) |
| Obligations related to assets sold under repurchase agreements | (12) | (468) | (480) | 377 | (136) | 241 |
| Subordinated debentures | — | (4) | (4) | 104 | (38) | 66 |
| Other interest-bearing liabilities | 87 | (19) | 68 | — | — | — |
| Total interest expense | 1,008 | (4,284) | (3,276) | 1,655 | (1,695) | (40) |
| Net interest income | \$ 571 | \$ 78 | \$ 649 | \$ 784 | \$ 458 | \$ 1,242 |

(1) Volume/rate variance is allocated on the percentage relationship of changes in balances and changes in rates to the total net change in net interest income on a taxable equivalent basis.

Other income

As shown in Table 11 on page 41A, other income was up \$347 million, or 4%, from 2001, while core other income, which excludes special items shown in Table 6 on page 27A, was up \$792 million or 10%, both reflecting recent U.S. acquisitions. Core other income was up 11% in RBC Banking, 4% in RBC Insurance and 30% in RBC Investments, largely reflecting acquisitions. Core other income was up 8% in RBC Global Services but was down 10% in RBC Capital Markets.

Excluding the impact of recent U.S. acquisitions, core other income was down \$183 million or 3%.

Partially driven by recent U.S. acquisitions, capital market fees (consisting of fees from full-service brokerage, discount brokerage and the institutional business) were up 23%, deposit and payment service charges were up 17% and investment management and custodial fees were up 8%. Mortgage banking revenues (which relate to mortgages originated in the U.S.) rose 8%, mutual fund revenues were up 4% and securitization revenues were up 41%, reflecting \$3.7 billion of residential mortgage securitizations during the year. Card service revenues were

up 8%. Despite contributions from recent U.S. acquisitions, trading revenues were down 3%. Insurance revenues were up 1% while credit fees declined 6%. Other – other income was up \$169 million, or 53%, largely the result of a \$77 million increase in fee revenue at RBC Dain Rauscher for the provision of back office services to other brokerage firms and a \$19 million increase in fee revenue at RBC Liberty Insurance for the provision of back office services to other insurance companies.

Excluding the effect of recent U.S. acquisitions, deposit and payment service charges increased by \$82 million, securitization revenues increased by \$51 million, insurance revenues increased by \$27 million, mutual fund revenues increased by \$8 million, credit fees declined by \$17 million, capital market fees declined by \$23 million, investment management and custodial fees declined by \$77 million and trading revenues declined by \$302 million.

Other income accounted for 54% of total revenues, unchanged from 2001.

TABLE 11 Other income

| (\$ millions, except percentage amounts) | 2002 | 2001 | 2000 | 2002 vs 2001 Increase (decrease) | |
|---|-----------------|-----------------|-----------------|-------------------------------------|-------------|
| Capital market fees | \$ 1,866 | \$ 1,523 | \$ 1,538 | \$ 343 | 23% |
| Trading revenues | 1,766 | 1,820 | 1,540 | (54) | (3) |
| Investment management and custodial fees | 1,179 | 1,096 | 860 | 83 | 8 |
| Deposit and payment service charges | 1,041 | 887 | 756 | 154 | 17 |
| Mutual fund revenues | 723 | 692 | 624 | 31 | 4 |
| Card service revenues | 496 | 458 | 420 | 38 | 8 |
| Foreign exchange revenues, other than trading | 279 | 312 | 299 | (33) | (11) |
| Credit fees | 223 | 237 | 212 | (14) | (6) |
| Mortgage banking revenues | 222 | 206 | — | 16 | 8 |
| Insurance revenues | 204 | 201 | 191 | 3 | 1 |
| Securitization revenues | 174 | 123 | 115 | 51 | 41 |
| Gain (loss) on disposal of premises and equipment | 15 | 22 | (16) | (7) | (32) |
| Loss on sale of securities | (116) | (128) | (11) | 12 | 9 |
| Other | 490 | 321 | 204 | 169 | 53 |
| Total core | 8,562 | 7,770 | 6,732 | 792 | 10 |
| Special items (1) | — | 445 | — | (445) | n.m. |
| Total | \$ 8,562 | \$ 8,215 | \$ 6,732 | \$ 347 | 4% |

(1) Special items in 2001 are described in Table 6 on page 27A. There were no special items for 2000 and 2002.

n.m. not meaningful

TABLE 12 Trading revenues

| (\$ millions) | 2002 | 2001 | 2000 |
|------------------------------------|-----------------|-----------------|-----------------|
| Net interest income (1) | \$ 127 | \$ (68) | \$ (365) |
| Other income (2) | 1,766 | 1,820 | 1,540 |
| Total | \$ 1,893 | \$ 1,752 | \$ 1,175 |
| By product | | | |
| Equity | \$ 753 | \$ 684 | \$ 495 |
| Fixed income and money markets (3) | 876 | 726 | 378 |
| Foreign exchange contracts (4) | 263 | 340 | 301 |
| Commodity and precious metals | 1 | 2 | 1 |
| Total | \$ 1,893 | \$ 1,752 | \$ 1,175 |

(1) Includes interest earned on trading securities and other cash instruments held in the trading portfolios less funding costs associated with trading-related derivative and security positions.

(2) Primarily includes realized and unrealized gains and losses on trading securities, derivative instruments and foreign exchange trading activities.

(3) Includes Canadian government securities and corporate debt instruments, swaps, interest rate options, interest rate futures, forward rate agreements.

(4) Includes foreign exchange spot, forward, futures and options contracts.

Trading revenues

Trading revenues include gains and losses on securities and derivatives that arise from market-making, sales and principal trading activities. These securities and derivative positions are marked-to-market on a daily basis. A description of trading revenues included in net interest income and other income is provided in footnotes (1) and (2) in Table 12 above.

As shown in Table 12, total trading revenues were up \$141 million or 8% in 2002. This was partially due to the acquisition of Tucker Anthony Sutro on October 31, 2001. Proprietary trading activities are strictly managed in accordance with VAR and trading limits and we continue to conduct the majority of client-related trading in the major G7 markets and currencies.

Fixed income and money market trading revenues increased by \$150 million, or 21%, largely from increases in fixed income trading volumes due to the favourable interest rate environment provided by successive central bank rate cuts and increases in derivative trading activities. Equity trading revenues increased by \$69 million, or 10%, primarily due to the inclusion of revenues from Tucker Anthony Sutro. Foreign exchange contract trading revenues declined by \$77 million, or 23%, in part due to lower trading volumes caused by increased volatility in the foreign exchange markets.

Financial priority: Cost control

Highlights

- Non-interest expense up 7% from 2001 and core non-interest expense up 8%, reflecting recent U.S. acquisitions
- Operating non-interest expense excluding recent U.S. acquisitions down 5%, reflecting continued cost control efforts

As shown in the table below, non-interest expense was up \$665 million or 7% and core non-interest expense (i.e., excluding special items shown in Table 6 on page 27A) was up \$756 million or 8% from 2001.

Operating non-interest expense (which excludes the special items mentioned in Table 6 on page 27A, the costs of SARs and retention compensation associated with acquisitions) was up \$753 million or 8% in 2002.

Non-interest expense of recent U.S. acquisitions was \$2.7 billion, up \$1.1 billion in 2002. The large increase is primarily due to the inclusion of a full year of expenses for RBC Centura, which was acquired on June 5, 2001, and expenses relating to the acquisition of Tucker Anthony Sutro, which was acquired on October 31, 2001. Excluding recent U.S. acquisitions, operating non-interest expense was down \$370 million or 5% from 2001. Further excluding goodwill amortization expense not associated with recent U.S. acquisitions, operating non-interest expense was down \$227 million, or 3%, in 2002.

From a segment perspective, by excluding expenses of recent U.S. acquisitions, operating expenses for RBC Investments would have been down \$135 million or 9%, for RBC Banking down \$109 million or 3% and for RBC Insurance up \$24 million or 13%. The decline in RBC Banking's expenses reflects ongoing success with its cost control initiatives initially implemented in 1999, while the reduction in RBC Investments largely reflects lower variable compensation in the weaker capital markets environment and cost control efforts. The increase in RBC Insurance expenses partially reflects the inclusion of an additional two months of expenses at RBC Liberty Insurance and higher staff costs.

Operating expenses for RBC Capital Markets were down \$140 million or 8%, whereas operating expenses at RBC Global Services were up \$66 million or 11%. The reductions at RBC Capital markets, similar to the reductions at RBC Investments, were the result of lower variable compensation and continuing cost control. The increase in RBC Global Services costs was affected by a change that became effective November 2001, pertaining to the classification of services provided by us to Moneris Solutions, a card processing joint venture in which we have a 50% interest. Payments for services provided to Moneris Solutions are now being treated as revenues, whereas previously they were treated as cost recoveries. Also, expenses were impacted by the July 2001 acquisition of Perpetual Fund Services. Excluding this acquisition, and

the change in classification of services provided to Moneris Solutions, operating expenses at RBC Global Services increased by 5%.

Human resources costs increased by \$614 million or 11% in 2002, largely the result of a \$476 million or 17% increase in salaries expense and a \$96 million or 14% increase in benefits expense. The increase in salaries expense is primarily due to the acquisitions of RBC Centura and Tucker Anthony Sutro. Pension benefit expense increased by \$129 million this year primarily due to a decrease in the fair value of plan assets due to weak equity markets, settlement costs on pension-related matters with Royal Trust pension plan members and increases in the interest cost on the benefit obligation. Furthermore, our defined contribution pension expenses were higher due to changes to our U.S. plan design and the launch of our Canadian defined contribution plan.

Other postretirement benefits expense decreased by \$39 million this year primarily as a result of an \$87 million charge that was taken in 2001 following the review of certain pension and other related future benefit plans. No similar charge was taken this year.

Retention compensation costs declined by \$18 million to \$158 million despite the addition of \$45 million of retention compensation costs pertaining to Tucker Anthony Sutro. We expect total retention compensation costs to fall to approximately \$87 million in 2003 and \$53 million in 2004. SAR expenses rose slightly during the year. SARs are discussed in Note 16 on pages 88A and 89A, and their costs are determined based upon the change in our share price and the vesting, which occurs over time.

Communications costs increased by \$115 million or 17%, equipment costs were up \$91 million or 12% and occupancy costs increased by \$72 million or 10%. These increases largely relate to the inclusion of a full year of expenses for RBC Centura Bank, which was acquired on June 5, 2001 and Tucker Anthony Sutro, which was acquired on October 31, 2001.

Excluding expenses from recent U.S. acquisitions, equipment costs would have been up \$61 million or 10%, human resource costs down \$139 million or 3%, amortization of goodwill and other intangibles down \$140 million or 86%, other costs down \$108 million or 11%, occupancy costs down \$24 million or 4%, professional fees down \$24 million or 8% and communications costs would have been up \$4 million or 1%.

TABLE 13 Operating non-interest expense

| (\$ millions) | 2002 | 2001 | 2002 vs 2001 Increase (decrease) | |
|--|-----------|----------|-------------------------------------|------|
| Non-interest expense | \$ 10,420 | \$ 9,755 | \$ 665 | 7% |
| Less: Special items (1) | — | (91) | (91) | n.m. |
| Core non-interest expense | 10,420 | 9,664 | 756 | 8 |
| Less: Costs of SARs | (44) | (23) | 21 | 91 |
| RBC Dain Rauscher retention compensation (2) | (158) | (176) | (18) | (10) |
| Operating expenses | 10,218 | 9,465 | 753 | 8 |
| Less: Non-interest expense of recent U.S. acquisitions (3) | (2,732) | (1,609) | 1,123 | 70 |
| Operating expenses, excluding recent U.S. acquisitions | 7,486 | 7,856 | (370) | (5) |
| Less: Amortization of goodwill not associated with recent U.S. acquisitions (3) | — | (143) | (143) | n.m. |
| Operating expenses, excluding recent U.S. acquisitions and goodwill amortization | 7,486 | 7,713 | (227) | (3)% |

(1) Special items in 2001 are described in Table 6 on page 27A. There were no special items in 2002.

(2) Includes Dain Rauscher Wessels for both periods and Tucker Anthony Sutro in 2002 only.

(3) Represents non-interest expense of RBC Centura Banks (now includes Eagle Bancshares, RBC Mortgage for the purposes of this discussion and analysis and what was previously SFNB), RBC Liberty Insurance and RBC Dain Rauscher (includes Tucker Anthony Sutro) including goodwill amortization expense of \$105 million in 2001 (nil in 2002), but excluding retention compensation costs and Dain Rauscher Wessels, which was integrated into RBC Capital Markets in early 2002.

n.m. not meaningful.

Outlook

In 2003, we expect to grow operating expenses at a lower rate than operating revenues.

TABLE 14 Non-interest expense

| (\$ millions, except percentage amounts) | 2002 | 2001 | 2000 | 2002 vs 2001 Increase (decrease) | |
|--|-----------|----------|----------|-------------------------------------|------|
| Human resources | | | | | |
| Salaries | \$ 3,224 | \$ 2,748 | \$ 2,319 | \$ 476 | 17% |
| Variable compensation | 2,095 | 2,056 | 1,839 | 39 | 2 |
| Acquisition related retention compensation | 158 | 176 | — | (18) | (10) |
| Benefits | 794 | 698 | 441 | 96 | 14 |
| SARs | 44 | 23 | 52 | 21 | 91 |
| | 6,315 | 5,701 | 4,651 | 614 | 11 |
| Occupancy | | | | | |
| Net premises rent | 595 | 561 | 384 | 34 | 6 |
| Premises repairs and maintenance | 70 | 55 | 68 | 15 | 27 |
| Depreciation | 103 | 91 | 81 | 12 | 13 |
| Property taxes | 11 | 6 | 15 | 5 | 83 |
| Energy | 17 | 11 | 22 | 6 | 55 |
| | 796 | 724 | 570 | 72 | 10 |
| Equipment | | | | | |
| Office and computer rental and maintenance | 516 | 431 | 376 | 85 | 20 |
| Depreciation | 304 | 298 | 289 | 6 | 2 |
| | 820 | 729 | 665 | 91 | 12 |
| Communications | | | | | |
| Telecommunication | 361 | 290 | 225 | 71 | 24 |
| Marketing and public relations | 211 | 180 | 173 | 31 | 17 |
| Postage and courier | 121 | 108 | 170 | 13 | 12 |
| Stationery and printing | 108 | 108 | 127 | — | — |
| | 801 | 686 | 695 | 115 | 17 |
| Professional fees | 419 | 391 | 267 | 28 | 7 |
| Amortization of goodwill | — | 248 | 76 | (248) | n.m. |
| Amortization of other intangibles | 72 | 36 | 11 | 36 | 100 |
| Other | | | | | |
| Business and capital taxes | 129 | 171 | 134 | (42) | (25) |
| Travel and relocation | 144 | 121 | 85 | 23 | 19 |
| Employee training | 46 | 43 | 38 | 3 | 7 |
| Donations | 41 | 35 | 26 | 6 | 17 |
| Other | 837 | 779 | 363 | 58 | 7 |
| | 1,197 | 1,149 | 646 | 48 | 4 |
| Total core | 10,420 | 9,664 | 7,581 | 756 | 8 |
| Special items (1) | — | 91 | — | (91) | n.m. |
| Total | \$ 10,420 | \$ 9,755 | \$ 7,581 | \$ 665 | 7% |

(1) Special items in 2001 are described in Table 6 on page 27A. There were no special items for 2000 and 2002.
n.m. not meaningful

Continuing our focus on cost control

The cost control initiatives undertaken in 2002 and in prior years are continuing to yield favourable results as reflected in the 5% decline in operating expenses, excluding recent U.S. acquisitions, shown in Table 13.

RBC Banking surpassed its stated objective of no non-interest expense growth in 2002, reducing non-interest expense by \$100 million or 3%, excluding recent U.S. acquisitions. Its success is due to favourable results from a number of initiatives, including the following.

Increasing focus on fraud prevention. This led to over \$50 million of savings realized this year.

Eliminating duplication and other process inefficiencies. As the result of integrating the credit card business into RBC Royal Bank's product and sales structure, over \$10 million in cost savings were realized during 2002.

Integration of certain functions of SFNB, RBC Builder Finance and RBC Mortgage into RBC Centura. The successful integration of certain functions resulted in the realization of 100% of the three-year cost savings target of US\$70 million, nearly two years ahead of schedule.

Integration of certain functions of RBC Centura into RBC Royal Bank. A portion of RBC Centura call centre services has been reallocated to the RBC Royal Bank call centres in Canada, whereby over half of RBC Centura inbound calls are now handled by call centres in Canada. RBC Centura is also expecting to realize over \$7 million of cost savings in 2003 from the integration of certain operations of Eagle Bancshares.

Moving into 2003, RBC Banking is developing a common business framework enabled by e-technologies. We believe that this streamlined model will drive transformational cost reductions by providing standardized and flexible solutions across segments, channels and products. This initiative is expected to generate cost savings commencing in 2004.

During 2002, RBC Insurance realized cost savings by insourcing the provision of technology and infrastructure support to the RBC Systems & Technology group and by outsourcing its payroll function to an external payroll service provider. Also, RBC Liberty Insurance completed the migration and consolidation of the business insurance software and outsourcing assets acquired from Genelco, resulting in cost eliminations. RBC Liberty Insurance is also in the process of migrating to the desktop and server operating environments used by the rest of our enterprise. These changes will result in lower costs and will leverage best practices.

RBC Investments' cost-cutting program, initiated in 2001 to offset the effects of market weakness, will continue into 2003. This segment continues to seek ways to permanently reduce non-interest expense. For example, by working with the Institutional & Investor Services unit of RBC Global Services, RBC Global Private Banking was able to realize cost savings through the sourcing of its fund management processing.

RBC Dain Rauscher achieved cost savings from the continued integration of Tucker Anthony Sutro. Cost savings are being realized through a number of initiatives, including reducing overlapping positions and leveraging scale opportunities that already exist in RBC Dain Rauscher's platform. RBC Dain Rauscher also achieved cost savings through the rationalization of parts of its business in response to poor market conditions. To date, cost savings realized from these initiatives have exceeded US\$30 million. Cost savings pertaining to the completion of the integration of Tucker Anthony Sutro into RBC Dain Rauscher are expected to be another US\$30 million in 2003.

RBC Capital Markets maintained a focused cost control effort in 2002 in response to the continued weak market conditions. Expense reductions were achieved through the execution of a number of initiatives including continued integration of Capital Market Services businesses in Canada and the U.S., targeted reductions in costs associated with the management of our loan portfolio, technology support and technology capital expenditures. In 2003, RBC Capital Markets will continue its focus on cost control.

RBC Global Services is a scale business with relatively high fixed costs. To achieve cost savings, this segment is focusing on improving operational efficiency by increasing revenue to achieve economies of scale and through continued improvements in its technology infrastructure. Revenue increases will be achieved through organic revenue growth and targeted acquisitions. Acquisitions will provide opportunities for cost savings through integration.

In addition to each platform undertaking its own cost containment initiatives, we have an E² (efficiency and effectiveness) effort underway for RBC Financial Group. The primary thrust of the E² initiative is to eliminate duplication between platforms and to identify centres of expertise that can be leveraged to enhance operational efficiency and revenue growth. To date, this initiative has identified over 55 projects that could result in cost savings and additional revenue.

TABLE 15 Taxes

(\$ millions, except percentage amounts)

| | 2002 | 2001 | 2000 |
|--------------------------------------|-----------------|-----------------|-----------------|
| Income taxes | | | |
| Consolidated statement of income | \$ 1,365 | \$ 1,340 | \$ 1,445 |
| Taxable equivalent adjustment | 40 | 32 | 28 |
| | 1,405 | 1,372 | 1,473 |
| Other taxes | | | |
| Goods and services and sales taxes | 224 | 221 | 208 |
| Payroll taxes | 245 | 237 | 188 |
| Provincial capital taxes | 107 | 146 | 108 |
| Property taxes (1) | 11 | 6 | 16 |
| Business taxes | 22 | 25 | 26 |
| Insurance premium taxes | 22 | 21 | 11 |
| | 631 | 656 | 557 |
| Total | \$ 2,036 | \$ 2,028 | \$ 2,030 |
| Effective income tax rate (2) | 32.2% | 34.7% | 38.6% |
| Effective total tax rate (3) | 41.5% | 44.6% | 46.9% |

(1) Includes amounts netted against other income regarding investment properties.

(2) Income taxes reported in the consolidated statement of income, as a percentage of net income before income taxes.

(3) Total income taxes and other taxes as a percentage of net income before income taxes and other taxes expressed on a taxable equivalent basis.

Income and other taxes

Income and other taxes shown in Table 15 above were \$2,036 million in 2002, comprising income taxes of \$1,405 million and other taxes of \$631 million. Income taxes increased by \$33 million from 2001, largely due to higher net income before tax. Other taxes declined by \$25 million largely as a result of a decrease in the amount of provincial capital taxes paid.

As shown above, the effective income tax rate decreased from 34.7% in 2001 to 32.2% in 2002, reflecting a reduction in federal and provincial tax rates in Canada.

In addition to the income and other taxes reported in the consolidated statement of income, the bank recorded income tax expense of \$125 million in 2002 (\$644 million income tax benefit in 2001) in shareholders' equity as shown in Note 14 on page 86A.

Financial priority: Strong credit quality

Highlights

- Business and government loans and acceptances decreased from 35% of total loans, acceptances and reverse repurchase agreements in 2001 to 32%
- Gross impaired loans down 7%
- Net impaired loans to total loans, acceptances and reverse repurchase agreements down slightly from .08% to .04%
- Provision for credit losses stable at \$1.1 billion
- Specific provision ratio of .51%, down slightly from .53%
- Net write-offs ratio of .60%, up from .47%
- Allowance for credit losses down slightly from \$2.4 billion to \$2.3 billion

Loan portfolio

During 2002, the loan portfolio performed well in a very challenging environment, reflecting changes we have made in credit practices over the last two years. In 2002, we continued our strategy of moving towards a lower-risk portfolio mix, which includes more residential mortgage loans and less corporate loans, which are riskier and more capital intensive. As shown in the charts below, business and government loans and acceptances decreased to 32% of total loans, acceptances and reverse repurchase agreements in 2002 from 43% in 1998. This compares to a ratio of 35% in 2001.

We buy credit protection to offset losses that may result from the potential credit deterioration of particular counterparties and to manage absolute exposure. As at October 31, 2002, we had \$1 billion of credit protection in place including \$2 billion in each of the telecommunication, energy and financial services sectors.

The portion of our business and government credit exposure rated investment grade increased slightly during 2002 from 69% to 70%. Business and government includes our small business portfolio, which is generally rated lower than larger businesses.

Table 16 on page 47A and Table 21 on page 52A provide a detailed breakdown of loans, acceptances and reverse repurchase agreements. Business and government loans and acceptances declined \$5.6 billion in Canada and \$1.7 billion internationally, with a \$2.3 billion reduction outside of the U.S., partially offset by a \$.6 billion increase in the U.S. The overall decrease is driven by the ongoing business strategy of exiting non-core client relationships in RBC Capital Markets. We do not engage in subprime lending in the U.S.

In Canada, there were no significant increases in any of the sectors other than the automotive sector where the increase was due to the reclassification of approximately \$.8 billion of loans from transportation and environment. The largest reduction was in energy (\$1.4 billion).

In the U.S., portfolio increases took place in energy (\$1.1 billion) and commercial real estate (\$.8 billion), partially offset by a decrease in

industrial products (\$.5 billion). The largest share of the increase in the energy sector was in power generation. The commercial real estate increase includes \$.2 billion of loans acquired as a result of the Eagle Bancshares acquisition.

Outside Canada and U.S., loans decreased by \$2.3 billion, including reductions in financial services, energy and industrial products. The overall reductions reflect focused de-marketing of Asia-Pacific loans, including Japan.

Telecommunication loans outstanding globally decreased by 22% to \$1.7 billion at October 31, 2002. Non-investment grade telecommunication loans were \$.9 billion, down from 59% of the portfolio to 49%. Currently seven telecommunication loans are classified as impaired, compared to six at October 31, 2001. Approximately 90% of the original impaired amount has been written-off or specifically provided for. This results in a net impaired amount of \$41 million, at the end of 2002.

At October 31, 2002, loans outstanding to the power generation sub-sector within the energy sector were \$2.0 billion, of which 48% were investment grade. The net impaired amount of \$74 million related to three accounts.

For additional discussion of loans, see the Balance sheet and capital management section on page 58A.

Impaired loans

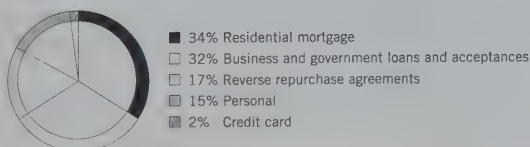
Loans are generally classified as impaired, meaning the accrual of interest is discontinued, under conditions described in Note 1 on page 72A.

As indicated in Table 17 on page 48A, gross impaired loans decreased \$177 million during the year to \$2,288 million. This decline reflects a slowdown in net additions (\$1,280 million versus \$1,912 million in 2001) and increased write-offs (\$1,457 million versus \$1,125 million in 2001).

Gross impaired loans decreased in both the consumer and the business and government loan portfolios.

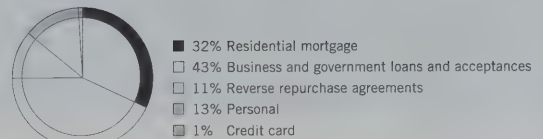
Breakdown of loans, acceptances and reverse repurchase agreements portfolio (2002)

Significant change...



Breakdown of loans, acceptances and reverse repurchase agreements portfolio (1998)

in portfolio mix



In the consumer portfolio, gross impaired loans decreased by \$67 million to \$437 million. Canada saw a large decrease (\$75 million), resulting from overall portfolio improvement due to recent initiatives such as the implementation of an advanced risk modeling technology in order to optimize risk-return and the optimization of credit policies and procedures (including the implementation of new origination models and new credit management and collection procedures).

Business and government gross impaired loans fell \$110 million to \$1,851 million. This consisted of reductions in Canada (\$276 million) and the U.S. (\$50 million), offsetting increases in other international (\$216 million). Gross impaired loans in the Canadian transportation and environment sector fell \$136 million due to a significant single name returning to performing status. There were also decreases in commercial real estate loans (\$72 million) and small business loans (\$56 million). The U.S. saw a net decrease resulting from reductions in the telecommunication sector (\$195 million), driven by significant write-offs. This decrease was partially offset by an increase in the energy and media and cable sectors. Each of these two sectors was impacted by single individual accounts. New impaired loans in Argentina contributed to an increase in other international.

As a percentage of related loans, acceptances and reverse repurchase agreements (after general allowance for loan losses) net impaired loans decreased slightly from .08% to .04%.

Provision for credit losses

The provision for credit losses is charged to income by an amount necessary to bring the allowance for credit losses to a level determined

appropriate by management, as discussed in the Allowance for credit losses section below.

The provision for credit losses was \$1,065 million in 2002, down \$54 million from 2001, as shown in Table 18 on page 49A.

We acquire credit protection on portions of our portfolio by entering into credit derivative contracts. We also provide protection through credit derivatives to various counterparties. This year's provision for credit losses included amounts related to a telecommunication account that was classified as impaired and was partially offset by gains of \$102 million on a related credit derivative. This amount was recorded in other income. We had also provided credit protection through derivatives to counterparties with respect to a large U.S. telecommunication company, which defaulted during the year, leading to a mark-to-market loss of \$69 million.

In the consumer portfolio, the specific provision increased by \$25 million to \$430 million. Business and government loans showed a slight decrease of \$9 million to \$635 million. This comprises decreases in Canada of \$166 million, partially offset by increases in the U.S. of \$52 million and other international of \$105 million. The decreases in Canada are spread across various industries. In the U.S., there was an increase in the energy and information technology sectors, partially offset by decreases in commercial real estate and telecommunication. The increase in U.S. energy (\$107 million) is due to a single account.

The specific provision amounted to .51% (.49% net of effect of credit derivatives) of average loans, acceptances and reverse repurchase agreements, down from .53% in 2001 and compared to a 2002 objective of .45%–.55%.

Outlook

In light of the continued economic and global political uncertainty that we face, we expect a specific provision for credit losses ratio of .45–.55% in 2003, which is unchanged from our 2002 objective.

Allowance for credit losses

The allowance for credit losses is maintained at a level that management believes is sufficient to absorb probable losses in the loan and off-balance sheet portfolios. The individual elements as well as the overall allowance are evaluated on a quarterly basis. This evaluation is based on continuing assessments of problem accounts, recent loss experience and changes in other factors, including the composition and quality of the portfolio, economic conditions and regulatory requirements. The allowance is increased by the provision for credit losses, which is charged to income, and decreased by the amount of write-offs net of recoveries.

The determination of the allowance for credit losses is based upon estimates derived from historical analysis, adjusted to take into account management's judgment relating to current assumptions. Therefore, the allowance for credit losses will inevitably differ from actual losses incurred in the future. To minimize these differences, management assesses the methodology and all significant assumptions on a regular basis.

The allowance for credit losses comprises three components – specific, general allocated and general unallocated – as described in Note 1 on page 73A.

As shown in Table 19 on page 50A, the allowance for credit losses decreased \$78 million or 3% between 2001 and 2002 to \$2,314 million. During the year, write-offs, net of recoveries, were \$1,259 million or .60% of average loans, acceptances, and reverse repurchase agreements versus \$940 million or .47% a year ago. The country risk allowance of \$31 million has been eliminated as a result of the write-off of the related fully provisioned loans.

In 2000, we entered into an agreement with an AAA rated reinsurer to provide capital if exceptional losses occur in the bank's loan portfolio. During the year, the reinsurer was downgraded from AAA. Based on this development and an internal review by management, the agreement was not renewed for fiscal 2003.

Credit risk concentrations

Concentration risk exists if a number of clients are engaged in similar activities, are located in the same geographic region or have comparable economic characteristics such that their ability to meet contractual obligations would be similarly affected by changes in economic, political or other conditions. Strategies to minimize concentration risk are discussed further under portfolio diversification in the Risk management section on page 55A. In terms of geographic risk, Table 16 on page 47A shows that the largest domestic geographic exposure is in Ontario, comprising 38% of total loans, acceptances and reverse repurchase agreements. Internationally, the largest concentration is in the U.S. where we have 15% of our total loans, acceptances and reverse repurchase agreements.

As shown in Table 16 on page 47A, excluding small business, the largest sector concentrations are in financial services, commercial real estate and energy, with 4%, 3% and 3% of loans, acceptances and reverse repurchase agreements, respectively.

Table 20 on page 51A illustrates geographic risk concentrations of contractual amounts with clients outside of Canada. Only 11% of contractual amounts with clients are outside Canada and the U.S.

TABLE 16 Loans, acceptances and reverse repurchase agreements (1)

| (\$ millions, except percentage amounts) | 2002 | 2001 | 2000 | 1999 | 1998 | 2002 | 1998 |
|---|-------------------|-------------------|-------------------|-------------------|-------------------|-------------|-------------|
| Canada | | | | | | | |
| Atlantic provinces (2) | \$ 9,770 | \$ 9,654 | \$ 9,690 | \$ 8,840 | \$ 8,052 | 4.5% | 4.5% |
| Quebec | 15,190 | 13,863 | 16,191 | 14,936 | 14,066 | 7.1 | 7.9 |
| Ontario | 82,689 | 92,966 | 73,124 | 67,120 | 64,566 | 38.4 | 36.3 |
| Prairie provinces (3) | 26,989 | 25,192 | 29,402 | 25,521 | 23,288 | 12.5 | 13.1 |
| British Columbia | 23,367 | 22,696 | 25,118 | 23,141 | 22,295 | 10.9 | 12.5 |
| Total Canada | 158,005 | 164,371 | 153,525 | 139,558 | 132,267 | 73.4 | 74.3 |
| Consumer | | | | | | | |
| Residential mortgage | 67,700 | 64,066 | 61,444 | 58,524 | 56,437 | 31.5 | 31.7 |
| Personal | 25,918 | 27,202 | 27,207 | 24,353 | 21,814 | 12.0 | 12.3 |
| Credit card | 4,740 | 4,110 | 4,666 | 2,666 | 1,945 | 2.2 | 1.1 |
| | 98,358 | 95,378 | 93,317 | 85,543 | 80,196 | 45.7 | 45.1 |
| Business and government loans and acceptances | | | | | | | |
| Small business (4) | 9,470 | 9,788 | 11,701 | 10,334 | 8,452 | 4.4 | 4.7 |
| Agriculture | 4,427 | 4,758 | 4,931 | 4,217 | 3,851 | 2.1 | 2.2 |
| Financial services | 3,015 | 3,010 | 2,218 | 1,567 | 1,718 | 1.4 | 1.0 |
| Energy | 2,911 | 4,293 | 3,754 | 3,350 | 3,442 | 1.4 | 1.9 |
| Commercial mortgages | 2,468 | 2,635 | 2,961 | 2,635 | 2,434 | 1.1 | 1.4 |
| Commercial real estate | 2,393 | 2,325 | 2,594 | 2,400 | 2,523 | 1.1 | 1.4 |
| Consumer goods | 2,238 | 2,447 | 2,874 | 2,086 | 2,802 | 1.0 | 1.6 |
| Industrial products | 1,569 | 2,174 | 2,470 | 2,301 | 2,241 | .7 | 1.3 |
| Transportation and environment (5) | 1,450 | 2,138 | 1,519 | 1,562 | 1,392 | .7 | .8 |
| Automotive (5) | 1,370 | 864 | 673 | 611 | 698 | .6 | .4 |
| Government | 1,039 | 1,597 | 1,385 | 2,105 | 1,951 | .5 | 1.1 |
| Media and cable (6) | 994 | 1,510 | 1,120 | 1,135 | 959 | .5 | .5 |
| Forest products | 954 | 1,275 | 1,362 | 1,151 | 1,728 | .4 | 1.0 |
| Telecommunication | 487 | 677 | 1,008 | 525 | 361 | .2 | .2 |
| Mining and metals | 361 | 636 | 897 | 845 | 750 | .2 | .4 |
| Information technology | 191 | 203 | 210 | 191 | 204 | .1 | .1 |
| Other | 5,194 | 5,803 | 6,437 | 4,650 | 4,577 | 2.4 | 2.5 |
| | 40,531 | 46,133 | 48,114 | 41,665 | 40,083 | 18.8 | 22.5 |
| Reverse repurchase agreements | 19,116 | 22,860 | 12,094 | 12,350 | 11,988 | 8.9 | 6.7 |
| Total Canada | 158,005 | 164,371 | 153,525 | 139,558 | 132,267 | 73.4 | 74.3 |
| International | | | | | | | |
| United States | 32,442 | 29,879 | 15,939 | 17,247 | 17,728 | 15.1 | 10.0 |
| Europe, Middle East and Africa | 19,006 | 16,860 | 9,782 | 9,642 | 16,822 | 8.8 | 9.5 |
| Caribbean | 2,018 | 1,856 | 2,059 | 1,502 | 1,573 | .9 | .9 |
| Latin America | 1,400 | 1,680 | 1,842 | 2,309 | 3,875 | .6 | 2.2 |
| Asia | 1,004 | 1,328 | 1,781 | 2,417 | 4,550 | .5 | 2.5 |
| Australia and New Zealand | 1,468 | 1,207 | 1,218 | 1,693 | 1,085 | .7 | .6 |
| Total international | 57,338 | 52,810 | 32,621 | 34,810 | 45,633 | 26.6 | 25.7 |
| Consumer | | | | | | | |
| Residential mortgage | 5,140 | 3,376 | 1,540 | 718 | 632 | 2.4 | .4 |
| Personal | 6,038 | 5,309 | 812 | 902 | 947 | 2.8 | .5 |
| Credit card | 174 | 173 | — | — | — | .1 | — |
| | 11,352 | 8,858 | 2,352 | 1,620 | 1,579 | 5.3 | .9 |
| Business and government loans and acceptances | | | | | | | |
| Financial services | 6,542 | 9,347 | 7,912 | 6,937 | 10,896 | 3.0 | 6.1 |
| Energy | 3,731 | 2,994 | 3,051 | 3,887 | 4,702 | 1.7 | 2.6 |
| Commercial real estate | 5,124 | 4,082 | 271 | 464 | 862 | 2.4 | .5 |
| Consumer goods | 1,383 | 1,699 | 1,111 | 1,411 | 2,756 | .6 | 1.5 |
| Industrial products | 1,199 | 2,116 | 1,749 | 1,325 | 1,881 | .6 | 1.1 |
| Transportation and environmental | 2,442 | 1,571 | 1,487 | 1,975 | 2,296 | 1.1 | 1.3 |
| Automotive | 411 | 527 | 513 | 878 | 2,264 | .2 | 1.3 |
| Government | 130 | 128 | 167 | 773 | 492 | .1 | .3 |
| Media and cable (6) | 1,321 | 1,380 | 2,033 | 1,909 | 2,270 | .6 | 1.3 |
| Forest products | 417 | 385 | 468 | 549 | 609 | .2 | .3 |
| Telecommunication | 1,246 | 1,558 | 2,244 | 1,206 | 1,756 | .6 | 1.0 |
| Mining and metals | 1,192 | 1,071 | 901 | 881 | 1,323 | .6 | .7 |
| Information technology | 180 | 396 | 433 | 709 | 1,212 | .1 | .7 |
| Other | 3,953 | 3,688 | 1,720 | 2,364 | 2,816 | 1.8 | 1.6 |
| | 29,271 | 30,942 | 24,060 | 25,268 | 36,135 | 13.6 | 20.3 |
| Reverse repurchase agreements | 16,715 | 13,010 | 6,209 | 7,922 | 7,919 | 7.7 | 4.5 |
| Total international | 57,338 | 52,810 | 32,621 | 34,810 | 45,633 | 26.6 | 25.7 |
| Total loans, acceptances and reverse repurchase agreements | 215,343 | 217,181 | 186,146 | 174,368 | 177,900 | 100% | 100% |
| Allowance for loan losses | (2,203) | (2,278) | (1,871) | (1,884) | (2,026) | | |
| Total | \$ 213,140 | \$ 214,903 | \$ 184,275 | \$ 172,484 | \$ 175,874 | | |

(1) Based on residence of borrower.

(2) Includes Newfoundland and Labrador, Prince Edward Island, Nova Scotia and New Brunswick.

(3) Includes Manitoba, Saskatchewan and Alberta.

(4) Small business loans in 2002 comprises the following industries: commercial real estate of \$1,737 million (2001 – \$1,788 million); consumer goods of \$1,583 million (2001 – \$1,665 million); industrial products of \$887 million (2001 – \$916 million); transportation and environmental of \$552 million (2001 – \$605 million); automotive of \$377 million (2001 – \$434 million); forest products of \$278 million (2001 – \$296 million); energy of \$125 million (2001 – \$157 million); information technology of \$93 million (2001 – \$133 million); mining and metals of \$69 million (2001 – n.a.); financial services of \$132 million (2001 – \$96 million); media and cable of \$77 million (2001 – \$84 million); telecommunication of \$34 million (2001 – \$45 million); and other of \$3,526 million (2001 – \$3,569 million).

(5) Commencing in 2002, certain amounts were reclassified from transportation and environmental sector grouping to the automotive group.

(6) Includes cable loans of \$267 million in Canada in 2002 (2001 – \$330 million; 2000 – \$262 million; 1999 – \$169 million; 1998 – \$164 million) and \$634 million internationally in 2002 (2001 – \$625 million; 2000 – \$1,321 million; 1999 – \$850 million; 1998 – \$1,221 million).

TABLE 17 Impaired loans

| | 2002 | | 2001 | | 2000 | 1999 | 1998 |
|--|-----------------|-----------------|-----------------|-----------------|---------------|---------------|---------------|
| (\$ millions, except percentage amounts) | Gross | Net (1) | Gross | Net (1) | Net (1) | Net (1) | Net (1) |
| Canada | | | | | | | |
| Atlantic provinces (2) | \$ 107 | \$ 55 | \$ 124 | \$ 67 | \$ 65 | \$ 37 | \$ 24 |
| Quebec | 90 | 60 | 282 | 204 | 121 | 158 | 142 |
| Ontario | 471 | 261 | 621 | 330 | 287 | 190 | 80 |
| Prairie provinces (3) | 177 | 98 | 143 | 71 | 57 | 109 | 64 |
| British Columbia | 427 | 292 | 453 | 335 | 266 | 287 | 350 |
| Total Canada | 1,272 | 766 | 1,623 | 1,007 | 796 | 781 | 660 |
| Consumer | | | | | | | |
| Residential mortgage | 102 | 87 | 142 | 118 | 157 | 131 | 116 |
| Personal | 275 | 112 | 310 | 129 | 51 | 66 | 61 |
| | 377 | 199 | 452 | 247 | 208 | 197 | 177 |
| Business and government | | | | | | | |
| Small business (4) | 205 | 104 | 261 | 132 | 141 | 134 | 43 |
| Agriculture (4) | 141 | 97 | 111 | 86 | 39 | 49 | 31 |
| Financial services | - | (1) | 7 | 2 | 7 | 1 | (1) |
| Energy | 1 | 1 | 27 | 9 | - | 32 | 5 |
| Commercial mortgages | 17 | 8 | 22 | 5 | - | 7 | 5 |
| Commercial real estate | 23 | 11 | 95 | 44 | 41 | 109 | 69 |
| Consumer goods | 47 | 26 | 11 | 5 | 23 | 19 | 29 |
| Industrial products | 23 | 12 | 45 | 26 | 18 | 6 | 1 |
| Transportation and environment | 138 | 108 | 274 | 222 | 120 | 12 | 3 |
| Automotive | 10 | 3 | 18 | 5 | 4 | - | - |
| Media and cable | 18 | 6 | 43 | 15 | 17 | 30 | 23 |
| Forest products | 199 | 156 | 195 | 184 | 180 | 197 | 285 |
| Telecommunication | 20 | 6 | - | - | - | - | - |
| Mining and metals | - | - | 1 | 1 | (1) | (1) | - |
| Information technology | 6 | 2 | 11 | 7 | (2) | 2 | 8 |
| Other | 47 | 28 | 50 | 17 | 1 | (13) | (18) |
| | 895 | 567 | 1,171 | 760 | 588 | 584 | 483 |
| Total Canada | 1,272 | 766 | 1,623 | 1,007 | 796 | 781 | 660 |
| International | | | | | | | |
| United States | 584 | 355 | 626 | 375 | 69 | 25 | 15 |
| Latin America | 217 | 154 | 14 | 5 | 3 | 3 | 1 |
| Europe, Middle East and Africa | 115 | 50 | 79 | 35 | 7 | 12 | 24 |
| Caribbean | 71 | 52 | 55 | 39 | 26 | 28 | 31 |
| Australia and New Zealand | 26 | 17 | 23 | 19 | - | - | - |
| Asia | 3 | - | 14 | 3 | 2 | 35 | 54 |
| | 1,016 | 628 | 811 | 476 | 107 | 103 | 125 |
| LDCs | - | - | 31 | - | - | - | - |
| Total international | 1,016 | 628 | 842 | 476 | 107 | 103 | 125 |
| Consumer | | | | | | | |
| Residential mortgage | 29 | 26 | 37 | 35 | 5 | 6 | 7 |
| Personal | 31 | 17 | 15 | 8 | - | - | - |
| | 60 | 43 | 52 | 43 | 5 | 6 | 7 |
| Business and government | | | | | | | |
| Financial services | 77 | 46 | 83 | 24 | (2) | 22 | 15 |
| Energy | 242 | 139 | 3 | - | (2) | 3 | 4 |
| Commercial real estate | 75 | 62 | 81 | 49 | 1 | 4 | 10 |
| Consumer goods | 10 | 7 | 19 | 7 | - | 2 | 34 |
| Industrial products | 30 | 13 | 10 | (2) | 38 | 15 | 22 |
| Transportation and environment | 68 | 39 | 91 | 58 | 25 | - | 1 |
| Automotive | 29 | 22 | 33 | 25 | - | (3) | 10 |
| Media and cable (5) | 56 | 56 | - | - | - | - | - |
| Telecommunication | 77 | 35 | 272 | 122 | - | - | - |
| Mining and metals | 128 | 90 | 40 | 29 | 6 | 2 | - |
| Information technology | 48 | 17 | 76 | 70 | - | - | - |
| Other | 116 | 59 | 82 | 51 | 36 | 52 | 22 |
| | 956 | 585 | 790 | 433 | 102 | 97 | 118 |
| Total international | 1,016 | 628 | 842 | 476 | 107 | 103 | 125 |
| Total (6), (7) | \$ 2,288 | \$ 1,394 | \$ 2,465 | \$ 1,483 | \$ 903 | \$ 884 | \$ 785 |

(1) Net of specific allowance.

(2) Includes Newfoundland and Labrador, Prince Edward Island, Nova Scotia and New Brunswick.

(3) Includes Manitoba, Saskatchewan and Alberta.

(4) Includes government guaranteed portions of impaired loans of \$64 million in small business in 2002 (2001 - \$95 million; 2000 - \$101 million; 1999 - \$79 million) and \$10 million in agriculture (2001 - \$6 million; 2000 - \$6 million; 1999 - \$5 million). Prior to 1999, only the non-guaranteed portion was considered impaired.

(5) Consists entirely of cable impaired loans.

(6) Includes foreclosed assets of \$32 million in 2002 (2001 - \$37 million; 2000 - \$16 million; 1999 - \$26 million; 1998 - \$28 million).

(7) Past due loans greater than 90 days not included in impaired loans was \$217 million in 2002 (2001 - \$245 million).

TABLE 18 Provision for credit losses

| (\$ millions, except percentage amounts) | 2002 | 2001 | 2000 | 1999 | 1998 |
|--|-----------------|-----------------|---------------|---------------|---------------|
| Canada | | | | | |
| Atlantic provinces (1) | \$ 59 | \$ 63 | \$ 58 | \$ 32 | \$ 35 |
| Quebec | (5) | 43 | 22 | 71 | 63 |
| Ontario | 330 | 398 | 342 | 52 | 144 |
| Prairie provinces (2) | 86 | 81 | 64 | 95 | 53 |
| British Columbia | 59 | 104 | 40 | 192 | 132 |
| Total Canada | 529 | 689 | 526 | 442 | 427 |
| Consumer | | | | | |
| Residential mortgage | 3 | 8 | — | 4 | 9 |
| Personal | 266 | 265 | 301 | 172 | 171 |
| Credit card | 135 | 125 | 102 | 55 | 28 |
| | 404 | 398 | 403 | 231 | 208 |
| Business and government | | | | | |
| Small business | 110 | 164 | 105 | 113 | 48 |
| Agriculture | 22 | 20 | 4 | 2 | 4 |
| Financial services | (27) | (9) | — | 5 | 113 |
| Energy | 4 | 17 | (8) | 12 | 1 |
| Commercial mortgages | (5) | 7 | 2 | 8 | 6 |
| Commercial real estate | (15) | 15 | (17) | 9 | (30) |
| Consumer goods | 19 | 2 | 7 | 11 | 23 |
| Industrial products | (7) | 14 | 2 | (10) | (6) |
| Transportation and environment | (19) | 13 | 56 | 7 | (27) |
| Automotive | — | 17 | — | — | — |
| Media and cable | (7) | 13 | 12 | 8 | 4 |
| Forest products | 4 | 7 | (36) | 81 | 76 |
| Telecommunication | 59 | — | (1) | (32) | (29) |
| Mining and metals | (1) | — | (1) | 1 | — |
| Information technology | 3 | 3 | 8 | 8 | 5 |
| Other | (15) | 8 | (10) | (12) | 31 |
| | 125 | 291 | 123 | 211 | 219 |
| Total Canada | 529 | 689 | 526 | 442 | 427 |
| International | | | | | |
| United States | 440 | 377 | 99 | 45 | (7) |
| Latin America | 57 | 5 | 2 | 2 | (2) |
| Europe, Middle East and Africa | 38 | (1) | (9) | 21 | 10 |
| Caribbean | 6 | (6) | 3 | — | 3 |
| Australia and New Zealand | 5 | 4 | — | — | — |
| Asia | (10) | (19) | (50) | 20 | 124 |
| Total international | 536 | 360 | 45 | 88 | 128 |
| Consumer | | | | | |
| Residential mortgage | 7 | — | — | 1 | 1 |
| Personal | 15 | 5 | — | — | — |
| Credit card | 4 | 2 | — | — | — |
| | 26 | 7 | — | 1 | 1 |
| Business and government | | | | | |
| Financial services | 21 | (3) | (21) | 2 | 36 |
| Energy | 141 | (8) | (2) | — | 21 |
| Commercial real estate | 4 | 65 | 1 | 2 | (2) |
| Consumer goods | (2) | — | (7) | (10) | (5) |
| Industrial products | 5 | 3 | 34 | 31 | 9 |
| Transportation and environment | 21 | 8 | 42 | — | (1) |
| Automotive | 1 | 7 | (8) | (2) | 29 |
| Media and cable | — | 3 | — | — | — |
| Telecommunication | 202 | 272 | — | — | — |
| Mining and metals | 28 | — | 2 | 15 | — |
| Information technology | 41 | 7 | — | 3 | — |
| Other | 48 | (1) | 4 | 46 | 40 |
| | 510 | 353 | 45 | 87 | 127 |
| Total international | 536 | 360 | 45 | 88 | 128 |
| Total specific provision | 1,065 | 1,049 | 571 | 530 | 555 |
| Country risk provision | — | — | — | — | (80) |
| General allocated (3) | (22) | 205 | 73 | n.a. | n.a. |
| General unallocated (3) | 22 | (135) | 47 | n.a. | n.a. |
| Total general provision (3) | — | 70 | 120 | 230 | 100 |
| Total | \$ 1,065 | \$ 1,119 | \$ 691 | \$ 760 | \$ 575 |

(1) Includes Newfoundland and Labrador, Prince Edward Island, Nova Scotia and New Brunswick.

(2) Includes Manitoba, Saskatchewan and Alberta.

(3) The general allocated provision and the general unallocated provision together totalled \$230 million in 1999 and \$100 million in 1998. These were not separated into the general allocated and general unallocated components.

TABLE 19 Allowance for credit losses

| (\$ millions, except percentage amounts) | 2002 | 2001 | 2000 | 1999 | 1998 |
|---|-----------------|-----------------|-----------------|-----------------|-----------------|
| Allowance at beginning of year | \$ 2,392 | \$ 1,975 | \$ 1,900 | \$ 2,066 | \$ 2,118 |
| Provision for credit losses | 1,065 | 1,119 | 691 | 760 | 575 |
| Write-offs | | | | | |
| Canada | | | | | |
| Residential mortgage | (11) | (15) | (11) | (14) | (17) |
| Personal | (381) | (394) | (372) | (236) | (163) |
| Credit card | (172) | (169) | (150) | (65) | (52) |
| Business and government | (330) | (296) | (225) | (524) | (250) |
| | (894) | (874) | (758) | (839) | (482) |
| International | | | | | |
| Residential mortgage | (1) | (9) | — | — | — |
| Personal | (17) | (7) | — | — | — |
| Credit card | (6) | (2) | — | — | — |
| Business and government | (506) | (233) | (81) | (229) | (29) |
| LDC exposures | (33) | — | — | (4) | (325) |
| | (563) | (251) | (81) | (233) | (354) |
| | (1,457) | (1,125) | (839) | (1,072) | (836) |
| Recoveries | | | | | |
| Canada | | | | | |
| Residential mortgage | — | — | — | 2 | 6 |
| Personal | 68 | 66 | 44 | 31 | 26 |
| Credit card | 37 | 44 | 48 | 10 | 24 |
| Business and government | 72 | 58 | 48 | 66 | 80 |
| | 177 | 168 | 140 | 109 | 136 |
| International | | | | | |
| Personal | 2 | 1 | — | — | — |
| Credit card | 1 | — | — | — | — |
| Business and government | 18 | 16 | 22 | 5 | 8 |
| | 21 | 17 | 22 | 5 | 8 |
| | 198 | 185 | 162 | 114 | 144 |
| Net write-offs | (1,259) | (940) | (677) | (958) | (692) |
| Acquisition of Centura Banks | — | 157 | — | — | — |
| Acquisition Eagle Bancshares | 18 | — | — | — | — |
| Adjustments | 98 | 81 | 61 | 32 | 65 |
| Allowance at end of year | \$ 2,314 | \$ 2,392 | \$ 1,975 | \$ 1,900 | \$ 2,066 |
| Allocation of allowance (1) | | | | | |
| Canada | | | | | |
| Residential mortgage | \$ 35 | \$ 45 | \$ 46 | \$ 53 | \$ 50 |
| Personal | 429 | 447 | 403 | 344 | 156 |
| Credit card | 147 | 147 | 88 | 60 | — |
| Business and government | 711 | 791 | 664 | 748 | 604 |
| | 1,322 | 1,430 | 1,201 | 1,205 | 810 |
| International | | | | | |
| Residential mortgage | 6 | 4 | 11 | 9 | 7 |
| Personal | 36 | 33 | — | — | — |
| Credit card | 5 | 5 | — | — | — |
| Business and government | 583 | 581 | 322 | 380 | 359 |
| | 630 | 623 | 333 | 389 | 366 |
| Allocated allowance for loan losses (2) | 1,952 | 2,053 | 1,534 | 1,594 | n.a. |
| Unallocated allowance for loan losses (2) | 251 | 225 | 337 | 290 | n.a. |
| Total allowance for loan losses | 2,203 | 2,278 | 1,871 | 1,884 | 2,026 |
| Allowance for off-balance sheet and other items (3) | 109 | 109 | 98 | — | — |
| Allowance for tax-exempt securities | 2 | 5 | 6 | 16 | 40 |
| Total allowance for credit losses | \$ 2,314 | \$ 2,392 | \$ 1,975 | \$ 1,900 | \$ 2,066 |
| Percentage of loans to total loans (4), (5) | | | | | |
| Canada | | | | | |
| Residential mortgage | 32% | 30% | 33% | 34% | 32% |
| Personal | 12 | 12 | 15 | 14 | 12 |
| Credit card | 2 | 2 | 2 | 1 | 1 |
| Business and government | 26 | 30 | 32 | 32 | 32 |
| | 72 | 74 | 82 | 81 | 77 |
| International | 28 | 26 | 18 | 19 | 23 |
| Total | 100% | 100% | 100% | 100% | 100% |

- As a result of a change in methodology in 1999, the allowance for loan losses in 2002, 2001, 2000 and 1999 includes amounts for the general allocated allowance, which have been allocated to loan categories. These amounts total \$1,060 million (2001 – \$1,076 million; 2000 – \$765 million; 1999 – \$790 million) and have been allocated as follows: for Canada – residential mortgage \$20 million (2001 – \$21 million; 2000 – \$18 million; 1999 – \$11 million), personal \$266 million (2001 – \$266 million; 2000 – \$207 million; 1999 – \$174 million), credit card \$147 million (2001 – \$147 million; 2000 – \$88 million; 1999 – \$60 million), business and government \$386 million (2001 – \$385 million; 2000 – \$321 million; 1999 – \$370 million), and for International – residential mortgage \$3 million (2001 – \$2 million; 2000 and 1999 – nil), personal \$22 million (2001 – \$26 million; 2000 and 1999 – nil), credit card \$5 million (2001 – \$5 million; 2000 and 1999 – nil), business and government \$211 million (2001 – \$224 million; 2000 – \$131 million; 1999 – \$175 million). The amounts prior to 1999 do not include the general allocated allowance.
- The general allocated and the general unallocated allowance totalled \$850 million in 1998. These were not separated into the general allocated and general unallocated components prior to October 31, 1999.
- Commencing in 2000, the allowance for off-balance sheet and other items was separated and reported under other liabilities. Previously, the amount was included in the allowance for loan losses.
- Loans include acceptances and reverse repurchase agreements.
- Loans in Canada include all loans booked in Canada, regardless of the currency or residence of the borrower.

TABLE 20 Foreign outstandings (1)

| | 2002 | | 2001 | | 2000 | |
|---|------------|-------------------|------------|-------------------|-----------|-------------------|
| (\$ millions, except percentage amounts) | | % of total assets | | % of total assets | | % of total assets |
| United States – Banks | \$ 5,838 | | \$ 7,186 | | \$ 5,462 | |
| Government | 3,257 | | 3,834 | | 889 | |
| Other | 62,210 | | 49,172 | | 30,034 | |
| | 71,305 | 18.92% | 60,192 | 16.75% | 36,385 | 12.56% |
| Western Europe | | | | | | |
| United Kingdom – Banks | 7,179 | | 6,275 | | 4,347 | |
| Government | 295 | | 153 | | 26 | |
| Other | 5,719 | | 5,256 | | 5,791 | |
| | 13,193 | 3.50 | 11,684 | 3.25 | 10,164 | 3.51 |
| France – Banks | 2,061 | | 2,378 | | 2,379 | |
| Government | 86 | | 68 | | 45 | |
| Other | 831 | | 1,176 | | 1,552 | |
| | 2,978 | .79 | 3,622 | 1.01 | 3,976 | 1.37 |
| Germany – Banks | 5,344 | | 5,952 | | 5,471 | |
| Government | 318 | | 173 | | 1 | |
| Other | 381 | | 559 | | 643 | |
| | 6,043 | 1.60 | 6,684 | 1.86 | 6,115 | 2.11 |
| Netherlands | 2,271 | .60 | 2,218 | .62 | 1,300 | .45 |
| Switzerland | 1,714 | .45 | 1,362 | .38 | 1,687 | .58 |
| Other | 5,658 | 1.51 | 5,244 | 1.46 | 4,305 | 1.49 |
| | 31,857 | 8.45 | 30,814 | 8.58 | 27,547 | 9.51 |
| Central/Eastern Europe, Middle East and Africa | 247 | .07 | 469 | .13 | 645 | .22 |
| Latin America | | | | | | |
| Argentina | 146 | .04 | 193 | .06 | 324 | .11 |
| Brazil | 38 | .01 | 71 | .02 | 75 | .02 |
| Chile | 800 | .21 | 836 | .23 | 751 | .26 |
| Mexico | 493 | .13 | 696 | .19 | 343 | .12 |
| Other | 42 | .01 | 174 | .05 | 212 | .08 |
| | 1,519 | .40 | 1,970 | .55 | 1,705 | .59 |
| Caribbean | | | | | | |
| Bahamas | 1,453 | .38 | 1,520 | .42 | 1,549 | .54 |
| Other | 485 | .13 | 1,902 | .53 | 1,952 | .67 |
| | 1,938 | .51 | 3,422 | .95 | 3,501 | 1.21 |
| Asia | | | | | | |
| Japan – Banks | 321 | | 53 | | 634 | |
| Government | 2,426 | | 1,663 | | 1,599 | |
| Other | 64 | | 988 | | 1,000 | |
| | 2,811 | .75 | 2,704 | .75 | 3,233 | 1.12 |
| Singapore | 229 | .06 | 217 | .06 | 336 | .11 |
| South Korea | 405 | .11 | 449 | .13 | 338 | .11 |
| Other | 38 | .01 | 145 | .04 | 188 | .07 |
| | 3,483 | .93 | 3,515 | .98 | 4,095 | 1.41 |
| Australia and New Zealand | 2,842 | .75 | 2,335 | .65 | 1,775 | .61 |
| Allowance for loan losses (2) | (760) | (.20) | (728) | (.20) | (441) | (.15) |
| Total | \$ 112,431 | 29.83% | \$ 101,989 | 28.39% | \$ 75,212 | 25.96% |

- (1) Includes contractual amounts with clients in a foreign country related to: loans, accrued interest, acceptances, interest-bearing deposits with banks, securities, other interest-earning investments and other monetary assets including net revaluation gains on foreign exchange and derivative products. Local currency outstandings, whether or not hedged or funded by local currency borrowings, are included in country exposure outstandings. Foreign outstandings are reported based on location of ultimate risk.
- (2) The allowance for loan losses includes the international component of the specific, general allocated and general unallocated allowance. For years prior to 2002, the allowance for loan losses also includes the country risk allowance.

TABLE 21 U.S. loans, acceptances and reverse repurchase agreements and loan quality information ⁽¹⁾

| (\$ millions) | Loan balance | | | Gross impaired loans | | | Net impaired loans | | | Provision for credit losses | | |
|--|--------------|-----------|-----------|----------------------|--------|--------|--------------------|--------|-------|-----------------------------|--------|-------|
| | 2002 | 2001 | 2000 | 2002 | 2001 | 2000 | 2002 | 2001 | 2000 | 2002 | 2001 | 2000 |
| Consumer | | | | | | | | | | | | |
| Residential mortgage | \$ 4,351 | \$ 2,664 | \$ 845 | \$ 16 | \$ 24 | \$ - | \$ 13 | \$ 22 | \$ - | \$ 7 | \$ 8 | \$ - |
| Personal | 5,269 | 4,621 | 78 | 31 | 15 | - | 17 | 8 | - | 15 | 5 | - |
| Credit card | 125 | 128 | - | - | - | - | - | - | - | 4 | 2 | - |
| | 9,745 | 7,413 | 923 | 47 | 39 | - | 30 | 30 | - | 26 | 15 | - |
| Business and government loans and acceptances | | | | | | | | | | | | |
| Financial services | 3,770 | 4,104 | 4,521 | 46 | 30 | - | 35 | 23 | - | 11 | 7 | - |
| Energy | 2,680 | 1,613 | 1,582 | 95 | - | - | 29 | - | - | 107 | - | - |
| Commercial real estate | 4,531 | 3,773 | 44 | 75 | 81 | 4 | 62 | 49 | 1 | 5 | 66 | 2 |
| Consumer goods | 958 | 1,172 | 435 | 10 | 9 | - | 7 | 7 | - | 4 | 2 | - |
| Industrial products | 974 | 1,513 | 1,107 | 30 | 8 | 68 | 13 | (1) | 34 | 8 | 3 | 40 |
| Transportation and environmental | 484 | 788 | 469 | 36 | 48 | 56 | 28 | 26 | 25 | 5 | (4) | 42 |
| Automotive | 409 | 408 | 221 | 29 | 33 | - | 22 | 25 | - | 1 | 6 | - |
| Government | 19 | 23 | - | - | - | - | - | - | - | - | - | - |
| Media and cable (2) | 1,107 | 1,038 | 1,782 | 56 | - | - | 56 | - | - | - | 3 | - |
| Forest products | 223 | 98 | 181 | - | - | - | - | - | - | - | - | - |
| Telecommunication | 689 | 835 | 1,131 | 77 | 272 | - | 35 | 122 | - | 202 | 272 | - |
| Mining and metals | 70 | 45 | 104 | - | - | - | - | - | - | - | - | - |
| Information technology | 177 | 299 | 374 | 48 | 76 | - | 17 | 70 | - | 41 | 7 | - |
| Other | 3,348 | 3,089 | 541 | 35 | 30 | 17 | 21 | 24 | 9 | 30 | - | 15 |
| | 19,439 | 18,798 | 12,492 | 537 | 587 | 145 | 325 | 345 | 69 | 414 | 362 | 99 |
| Reverse repurchase agreements | 3,258 | 3,668 | 2,524 | - | - | - | - | - | - | - | - | - |
| | \$ 32,442 | \$ 29,879 | \$ 15,939 | \$ 584 | \$ 626 | \$ 145 | \$ 355 | \$ 375 | \$ 69 | \$ 440 | \$ 377 | \$ 99 |

(1) Based on residence of the borrower.

(2) Includes cable loans of \$522 million in 2002 (2001 - \$455 million; 2000 - \$1,162 million) and cable gross impaired loans of \$56 million in 2002.

TABLE 22 Risk profile

| (\$ millions, except percentage amounts) | 2002 | 2001 | 2000 | 1999 | 1998 |
|---|----------|----------|----------|----------|----------|
| Gross impaired loans | | | | | |
| Beginning of year | \$ 2,465 | \$ 1,678 | \$ 1,704 | \$ 2,001 | \$ 1,819 |
| Net additions | 1,280 | 1,912 | 813 | 743 | 628 |
| Write-offs and adjustments | (1,457) | (1,125) | (839) | (1,040) | (446) |
| End of year | \$ 2,288 | \$ 2,465 | \$ 1,678 | \$ 1,704 | \$ 2,001 |
| Allowance for credit losses | | | | | |
| Specific | \$ 894 | \$ 951 | \$ 747 | \$ 786 | \$ 1,176 |
| Country risk | - | 31 | 28 | 34 | 40 |
| General allowance (2) | | | | | |
| General allocated (2), (4) | 1,169 | 1,185 | 863 | 790 | n.a. |
| General unallocated (2) | 251 | 225 | 337 | 290 | n.a. |
| Total general allowance (2) | 1,420 | 1,410 | 1,200 | 1,080 | 850 |
| Total | \$ 2,314 | \$ 2,392 | \$ 1,975 | \$ 1,900 | \$ 2,066 |
| As a % of loans, acceptances and reverse repurchase agreements | 1.0% | 1.1% | 1.0% | 1.1% | 1.2% |
| As a % of impaired loans (coverage ratio), excluding LDCs | 96% | 93% | 112% | 112% | 103% |
| Net impaired loans as a % of related loans, acceptances and reverse repurchase agreements (1) | | | | | |
| Canada | | | | | |
| Residential mortgage | .13% | .18% | .26% | .22% | .21% |
| Personal | .43 | .48 | .19 | .27 | .28 |
| Business and government | 1.00 | 1.17 | .99 | 1.05 | .86 |
| International | .49 | .63 | .52 | .55 | .48 |
| | 1.05 | .85 | .33 | .32 | .31 |
| Total before general allowance for loan losses | .65 | .69 | .49 | .51 | .44 |
| Total after general allowance for loan losses | .04% | .08% | (.11)% | (.11)% | (.04)% |
| Provision for credit losses | | | | | |
| Specific | \$ 1,065 | \$ 1,049 | \$ 571 | \$ 530 | \$ 555 |
| Country risk | - | - | - | - | (80) |
| General provision (3) | | | | | |
| General allocated (3) | (22) | 205 | 73 | n.a. | n.a. |
| General unallocated (3) | 22 | (135) | 47 | n.a. | n.a. |
| Total general provision | - | 70 | 120 | 230 | 100 |
| Total | \$ 1,065 | \$ 1,119 | \$ 691 | \$ 760 | \$ 575 |
| As a % of related average loans, acceptances and reverse repurchase agreements | | | | | |
| Canada | | | | | |
| Residential mortgage | -.0% | .01% | -.0% | .01% | .02% |
| Personal | 1.00 | .94 | 1.12 | .71 | .76 |
| Credit card | 3.10 | 2.73 | 2.87 | 2.39 | 1.39 |
| Business and government | .21 | .52 | .22 | .40 | .37 |
| International | .34 | .45 | .36 | .32 | .31 |
| | .98 | .74 | .13 | .23 | .31 |
| Total specific provision | .51% | .53% | .32% | .30% | .31% |
| Total provision | .51% | .56% | .38% | .43% | .32% |
| Net write-offs (excluding LDCs) as a % of average loans, acceptances and reverse repurchase agreements | .58% | .47% | .38% | .54% | .21% |
| Net write-offs as a % of average loans, acceptances and reverse repurchase agreements | .60% | .47% | .38% | .55% | .39% |

(1) Loans in Canada include all loans booked in Canada, regardless of the currency or residence of the borrower.

(2) The general allowance was not separated into allocated and unallocated components prior to October 31, 1999.

(3) The general provision was not separated into allocated and unallocated components prior to November 1, 1999.

(4) Includes the allowance for off-balance sheet and other items.

Risk management

Overview

The risk management function strives to build shareholder value through leadership in the strategic management of risk. Priorities include:

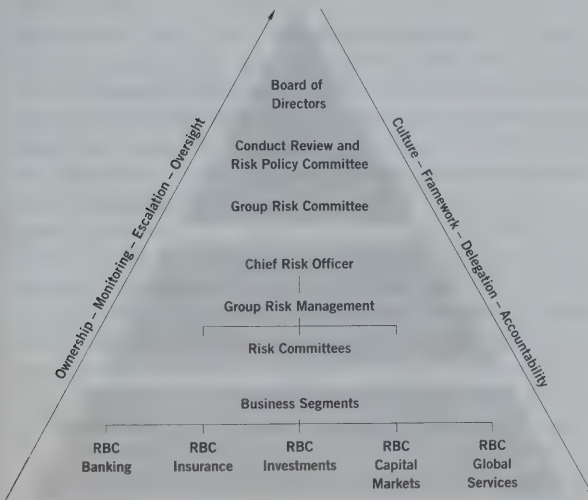
- Enhancing communication on risk and risk appetite throughout the organization
- Aligning the risk management function with our business segments
- Investing in our capabilities to better measure, understand and manage risk
- Strengthening the efficiency, accessibility and responsiveness of key risk processes and practices
- Attracting, developing and retaining a team of highly performing professionals

Our business activities expose us to the risks outlined in the risk pyramid below. We use the risk pyramid as the primary tool to identify and assess risk across the organization. It provides a common language for evaluating risk in business reviews, new business, new products, new initiatives, acquisitions or alliances. We pay particular attention to the more control-lable risks along the bottom of the pyramid.



- **Credit risk** is the risk of loss due to a counterparty's inability to fulfill its payment obligations. It also refers to a loss in market value due to the deterioration of a counterparty's financial position. A counterparty may be an issuer, debtor, borrower, policyholder, reinsurer or guarantor.
- **Market risk** is the risk of loss that results from changes in interest rates, foreign exchange rates, equity prices and commodity prices.
- **Liquidity risk** is the risk that we are unable to generate or obtain sufficient cash or equivalents on a cost-effective basis to meet our commitments as they fall due.
- **Insurance risk**, relative to our insurance platform, is the risk inherent in the development, issuance and administration of insurance policies, and includes product design and pricing risk, claims administration risk, underwriting risk and liability risk.
- **Operational risk** is the risk of direct or indirect loss resulting from inadequate or failed technology, human performance, processes or external events. The impact of operational risk can be financial loss, loss of reputation, loss of competitive position or legal and regulatory proceedings.

The Risk Pyramid: An organizational perspective



An organizational perspective

The cornerstone of effective risk management is a strong risk management culture, supported by numerous strategy and policy development processes, run jointly by risk management professionals and the business segments. This partnership is designed to ensure strategic alignment of business, risk and resource issues.

Risk management professionals work in partnership with the business segments and functional units to identify risks, which are then measured, monitored and managed. In line with a group-wide portfolio management approach, portfolio analytical techniques are employed in an effort to optimize the risk-reward profile and ensure the efficient allocation of capital.

A structure of management and board committees provides oversight of the risk management process.

The Board of Directors and Group Risk Committee

The top level of the organizational perspective risk pyramid on page 53A comprises the Board of Directors, the Conduct Review and Risk Policy Committee and Group Risk Committee. Key responsibilities are to:

- Shape, influence and communicate the organization's risk culture
- Determine and communicate the organization's risk appetite
- Define the organizational structure for Group Risk Management
- Review and approve policies for controlling risk
- Review and monitor the major risks being assumed by, or facing, the organization, providing direction as required
- Ensure there are sufficient and appropriate risk management resources across the organization against the risks being taken

Risk management

The middle level of the organizational perspective risk pyramid on page 53A comprises the Chief Risk Officer, Group Risk Management and the various Risk Committees. The Risk Committees include the Asset/Liability Committee, U.S. Corporate Governance Committee, the Ethics and Compliance Committee, Risk Management Committee and other committees responsible for areas such as interest rate risk and trading risk. During 2002, the SPE Risk Committee was established with a mandate to review and report on the activities of SPEs. This Committee reports jointly to the Chief Risk Officer and the Chief Financial Officer to ensure compliance with SPE policies and procedures across the enterprise. See page 64A for further discussion of SPEs.

Key responsibilities are to:

- Implement and maintain an integrated enterprise-wide risk measurement, management and reporting framework
- Establish a comprehensive risk assessment and approval process including enterprise-wide policies and procedures
- Establish guidelines and risk limits to ensure appropriate risk diversification and optimization of risk-return on both a portfolio and transactional basis
- Advise the board and executive management of major risks being assumed by, or facing, the organization
- Partner with the business segments in identifying, understanding, measuring, mitigating and monitoring the risks being taken

Economic Capital

Economic Capital (EC) is an estimate of the amount of equity required to underpin risks. It is calculated by determining the level of capital that is necessary to cover risks consistent with our desired solvency standard and debt ratings. EC analysis is intended to represent the shareholder's perspective and drives the optimization of shareholder returns. Calculation of EC involves a number of judgments and assumptions, and changes to them may result in different amounts of EC being computed.

EC is attributed to provide directly comparable performance measurements for each of our business activities and assist senior management in strategic planning, resource allocation and performance measurement. Capital attribution methodologies are continuously monitored to ensure risks are being consistently quantified utilizing all available information. Periodically, enhancements are made to these methodologies with the changes applied prospectively.

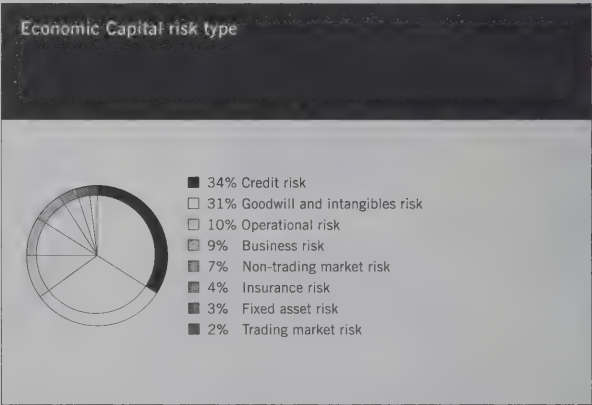
EC attribution methodology aims to:

- Cover all risks
- Ensure that a dollar of capital represents the same amount of risk wherever attributed
- Determine capital requirements in an unbiased accurate manner
- Create economically rational incentives for business managers

EC is a component in the calculation of Economic Profit (see page 26A). Capital attribution strengthens risk management discipline. EC is calculated for the following eight distinct risk types: credit risk, goodwill and intangibles risk, operational risk, business risk, non-trading market risk, insurance risk, fixed asset risk and trading market risk. Credit, market, insurance and operational risk are further detailed in the following sections. Business risk is the risk of loss due to variances in volumes, prices and costs caused by competitive forces, regulatory changes, and reputational and strategic risks. Goodwill and intangibles and fixed asset risks are defined as the risk that the value of these assets will be less than their net book value at a future date.

The combination of risk factors between and within risk categories and lines of business leads to some risk reduction, called diversification. These diversification benefits are passed on to our businesses. Therefore, Economic Profit and return on equity calculations are based on EC levels that include these diversification effects.

The following chart represents the proportionate EC levels by risk type for fiscal 2002.



The following sections discuss how we manage the major controllable risks including credit, market, liquidity, insurance and operational risk.

Credit risk

Credit risk is attributed to both on-balance sheet financial instruments such as loans and acceptances and credit equivalent amounts related to off-balance sheet financial instruments.

Our approach to credit risk management preserves the independence and integrity of risk assessment while being integrated into business management processes. Policies and procedures, which are communicated throughout the organization, guide the day-to-day management of credit risk exposure and are an essential part of our business culture. The goal of credit risk management is to evaluate and manage credit risk in order to further enhance this strong credit culture.

As discussed in the credit quality section on pages 45A to 52A, we have significantly enhanced our loan mix. This improvement is being achieved through our strategy of reducing exposure to non-core corporate client relationships while increasing the size of the consumer portfolio, including residential mortgages, which have very low loss rates.

We are continually adding to and improving the analytical tools used to analyze, measure and manage credit risk. This includes the use of third-party modeling tools, increased use of stress testing and enhanced management information systems.

Risk ratings

Corporate borrowers are assigned an internal risk rating based on a detailed examination of the organization. This examination considers industry sector trends, market competitiveness, overall company strategy,

financial strength, access to funds, financial management and any other risks facing the organization. Our rating system is based on a 22-point scale.

Credit scoring models are utilized to determine a credit score for consumer and certain small business lending. The credit scores measure the relative risk of the initial extension of credit and any further increases. Consumer credit risk is monitored using statistical scoring models and payment history in order to predict portfolio behaviour.

The internal risk ratings and credit scores are assessed and updated on a regular basis.

Portfolio diversification

Portfolio diversification is our overriding principle, therefore, our credit policies and limits are structured to ensure we are not overexposed to any given client, industry sector or geographic area.

To avoid excessive losses if any particular counterparty is unable to fulfill its payment obligations, we have established single name limits that are set according to risk ratings. In certain cases loans are syndicated in order to reduce overall exposure to a single name.

Limits are also in place to manage exposure to any particular country or sector. Each country and sector is assigned a risk rating. This risk rating considers factors common to all entities in a given country or sector yet outside the control of any individual entity. Limits are determined based on the risk rating along with our overall risk appetite and business strategy.

Risk mitigation

In order to mitigate risk on portions of our portfolio we enter into credit derivative contracts. As at October 31, 2002, credit mitigation was in place to cover \$1.0 billion in corporate credit exposure. We also provided protection through credit derivatives to various counterparties totalling \$3 billion as at October 31, 2002.

Loan sales are also used to mitigate risk. We seek to identify and sell loans we have made to borrowers whose risk and reward profile and borrower ratings are no longer desirable to us.

In order to respond proactively to credit deterioration and mitigate risk, a problem loan workout group with specialized expertise handles the management and collection of impaired loans as well as certain loans not currently impaired.

Market risk

The level of market risk to which we are exposed varies continually, reflecting changing market conditions, expectations of future price and market movements and the composition of our trading and non-trading portfolios. We have established risk management policies and limits for our trading and asset/liability management activities that allow us to monitor and control the exposure to market risk resulting from these activities. We conduct trading activities over-the-counter and on exchanges in the spot, forward, futures and options market and also participate in structured derivative transactions.

Interest rate risk

Interest rate risk is the potential adverse impact on our earnings and economic value due to changes in interest rates. In addition to the following discussion on trading activities please see the Non-trading portfolio section on page 61A.

Credit spread risk

Credit spread risk is the potential adverse impact on our earnings and economic value due to changes in credit worthiness of persons we have credit exposure to both specifically and market-wide. We are exposed to credit spread risk through our holdings of bonds and credit derivatives. In the trading portfolio, credit spread risk arises from market-making activity as well as through proprietary trading in our credit derivatives trading unit.

Foreign exchange rate risk

Foreign exchange rate risk is the potential adverse impact on our earnings and economic value due to currency rate movements. We are exposed to foreign exchange rate risk in both the spot and forward foreign exchange markets and in the derivative market.

Equity risk

Equity risk is the potential adverse impact on our earnings due to movements in individual equity prices or general movements in the value of the stock market. We are exposed to equity risk from the buying and selling of equities as a principal in our brokerage business and our investment activities. Equity risk also results from our trading activities, including the providing of tailored equity derivative transactions to clients, arbitrage trading and proprietary trading.

Trading activities

Market risks associated with trading activities are a result of market-making, positioning and sales and arbitrage activities in the interest rate, foreign exchange and equity markets. Our trading operation primarily acts as a market-maker or jobber, executing transactions that meet the financial requirements of our clients and transferring the market risks to the broad financial market. We also act as principal and take market risk proprietary positions within the authorizations granted by our Board of Directors.

We recently completed a major upgrade of our enterprise market risk management system as part of our continuous renewal process to implement best practices and enhance our risk oversight capabilities. This represents a significant milestone in our ability to assess potential for loss using modeling techniques across all risk classes in a consistent and timely manner. In November 2002, we received regulatory approval to use an internal models approach for the regulatory capital requirement on specific risk of investment grade debt portfolios.

Value-At-Risk

Market risks associated with trading activities are managed primarily through the use of Value-At-Risk (VAR) methodology. VAR is a generally accepted risk measurement concept that uses statistical models and historical market price information to estimate within a given level of confidence the maximum loss in market value that we would experience in our trading portfolios from an adverse one-day movement in market rates and prices. Our VAR measure is based on a 99% confidence level and is an estimate of the maximum potential trading loss in 99 out of every 100 days. We use a historical simulation of the previous 500 trading day scenarios to determine VAR for our trading portfolio. The graph on page 56A shows the daily net trading revenue compared to the global trading VAR amounts for the year ended October 31, 2002. Net trading revenue is defined as the sum of the mark-to-market adjustments booked on trading positions and net interest income accrued from trading assets. During fiscal 2002, we experienced only four days of net trading losses, and we did not experience a single day with net trading losses in excess of the VAR estimate for that day.

Table 23 on the following page shows the year-end, high, average and low VAR by major risk category for our combined trading activities for the years ended October 31, 2002 and 2001. The table also shows our global VAR, which incorporates the effects of correlation in the movements of interest rates, exchange rates, equity prices and commodity prices and the resulting benefits of diversification within our trading portfolio. As the table illustrates, the average VAR in 2002 was \$11 million, the same as the average VAR in 2001. An increase in the interest rate VAR (due to the inclusion of credit spread risk within the VAR model) was offset by a reduction in risk within the equity trading portfolio.

TABLE 23 Market risk measures – Trading activities (1)

| (\$ millions) | 2002 | | | | 2001 | | | |
|--|--------------|--------------|--------------|-------------|-------------|--------------|--------------|-------------|
| | Year-end | High | Average | Low | Year-end | High | Average | Low |
| Global VAR by major risk category | | | | | | | | |
| Equity | \$ 7 | \$ 12 | \$ 8 | \$ 6 | \$ 8 | \$ 16 | \$ 10 | \$ 6 |
| Foreign exchange and commodity | 2 | 9 | 3 | 1 | 2 | 6 | 3 | 1 |
| Interest rate | 11 | 14 | 6 | 2 | 3 | 9 | 4 | 2 |
| Global VAR (2) | \$ 13 | \$ 18 | \$ 11 | \$ 7 | \$ 8 | \$ 18 | \$ 11 | \$ 6 |

(1) Amounts are presented on a pre-tax basis and represent one-day VAR at a 99% confidence level.
(2) Global VAR reflects the correlation effect from each of the risk categories through diversification.

The Group Risk Management function, which is independent of the trading operations, is responsible for the daily measuring of global trading risk exposures. The function uses our VAR methodology to compare actual exposures to the limits established, to assess global risk-return trends and to alert senior management of adverse trends or positions. The function also develops and implements comprehensive risk measurement policies and risk limits that apply to trading activities.

We recognize that VAR is not an absolute measure of market risk and has its limitations since it is based on historical information only. In such circumstances, we implement other limits in order to control market liquidity risks, net position gap, term and volume for all products. This comprehensive market risk management framework is designed to ensure that an appropriate diversification of risks through policies is adopted on a global basis.

Back-testing

Back-testing against hypothetical profit and loss is used to monitor the statistical validity of VAR models. Hypothetical profit and loss is calculated by determining the impact of the actual one-day change in market rate or price movements on a given portfolio held constant for one day. Back-testing is performed daily across all trading portfolios. The results are submitted to OSFI on a quarterly basis. In fiscal 2002, there were two instances of the hypothetical net profit and loss exceeding the VAR. This is within the expected statistical range and supports the validity of the VAR model.

Stress testing

We also perform analysis on the potential trading losses due to stress events as a supplementary control on our market risk exposure. This is accomplished through applying historical and internally developed scenarios to the daily trading positions to monitor the effect of extreme market movements on the value of our portfolio.

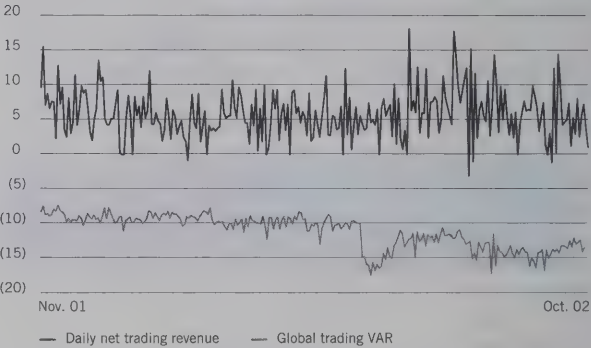
Liquidity risk

The objective of liquidity management is to ensure we have the ability to generate or obtain sufficient cash or its equivalents on a timely and cost-effective basis to meet our commitments as they fall due. The management of liquidity risk is crucial to protecting our capital, maintaining market confidence and ensuring that we can expand into profitable business opportunities.

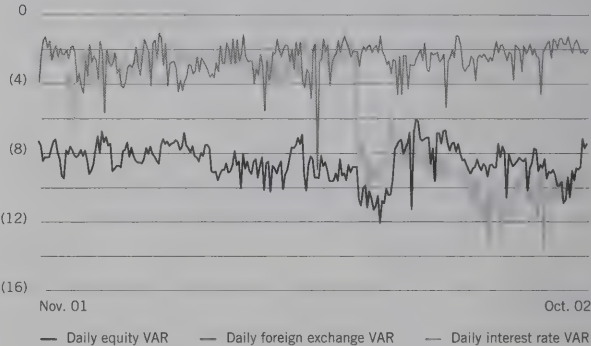
Liquidity risk is managed dynamically, exposures are continually measured, monitored and appropriately mitigated. We have developed and implemented a comprehensive liquidity management framework comprising policies, procedures, methodologies and measurements.

The Group Risk Committee and the Asset/Liability Committee provide guidance and oversight to our liquidity risk management program with the Audit Committee of the board approving our liquidity management framework and significant related policies. Corporate Treasury has global responsibility for developing liquidity management policies, strategies and contingency plans and for recommending and monitoring limits and coordinating subsidiary activities.

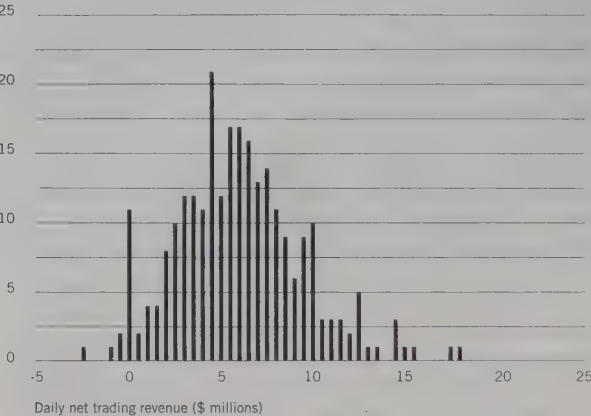
DAILY NET TRADING REVENUE VS GLOBAL TRADING VAR (\$ millions)



GLOBAL VAR BY MAJOR RISK CATEGORY (\$ millions)



HISTOGRAM OF DAILY NET TRADING REVENUE (number of days)



We have a Liquidity Crisis Team, composed of a cross-section of our senior executives. This team is responsible for the development, maintenance and success of our liquidity contingency plan. This plan would be activated in the event of a general market disruption or adverse economic developments that could destabilize our ability to meet obligations. This team meets regularly to review potential crisis scenarios and to update related action plans. Contingent liquidity exposures are identified and provisions are made to minimize possible damage through maintenance of a pool of unencumbered, high-quality assets. These assets are marketable and can be immediately sold or pledged for secured borrowing and represent a dedicated and reliable source of emergency funding. In addition, a segregated portfolio of eligible securities is continuously available to support our participation in Canadian payment and settlement systems. For further information on liquidity see the Liquidity management section on page 62A.

Insurance risk

Insurance risk includes product design and pricing risk, claims administration risk, underwriting risk and liability risk.

Product design and pricing risk

The process of designing and pricing products includes the estimation of many factors including future investment yields, mortality, morbidity, claims experience, expenses, policy lapse rates and taxes. Product design and pricing risk is the risk that actual experience will not match the assumptions made at the time pricing was determined and to the extent they differ, financial gains or losses will occur.

This risk is managed through detailed experience studies to support pricing assumptions and independent verification of scenario testing by our actuaries. In addition a portion of the policy benefit liabilities held on the balance sheet provides for misestimation and deterioration of assumptions from those assumed in the pricing. Risk is also mitigated through reinsurance, primarily for life insurance mortality and property and casualty catastrophe risks.

Claims administration risk

Claims administration risk is the exposure to higher than expected claims due to administrative practices in settling claims. Policies and procedures are in place that are designed to ensure that trained staff properly handle claims. There are approval limits in place to ensure that large dollar claims are handled and reviewed by experienced staff.

Underwriting risk

Underwriting risk is the exposure to financial losses resulting from the inappropriate selection and acceptance of the risks to be insured. Establishing policy retention limits that vary by market and geographic location mitigates exposure to large claims.

Liability risk

Liability risk exists when the attributes of a specific type of risk are misunderstood and improperly quantified and the liabilities established for this type of risk are inadequate. Actuaries review the assumptions used in the calculation of policy benefit liabilities on a quarterly basis. Provision for adverse deviations are included in the policy benefit liabilities to mitigate this risk.

Operational risk

Operational risk is the risk of direct or indirect loss resulting from inadequate or failed technology, human performance, processes or external events.

We endeavour to minimize operational losses by ensuring that effective infrastructure, controls, systems, and individuals are in place throughout our organization. We employ dedicated professionals who are proactive in developing and implementing new methodologies for the identification, assessment and management of operational risk.

We have developed and are currently implementing two new processes aimed at monitoring and mitigating operational risks in the organization.

Risk and control self-assessment (RCSA)

RCSA is a formal process of proactively identifying, documenting, assessing and managing our operational risks. Each business segment and functional unit is divided into its component activities, which become entities to be assessed. Each entity completes a workshop-based, self-assessment to determine their key risks, mitigating controls, the potential impact and likelihood of a problem occurring and the acceptability of the residual risk after existing controls are considered.

Where residual risk is deemed unacceptable, the group will agree on an action plan and timeline. The findings of the various RCSAs conducted are documented, aggregated, analyzed and reported on a group-wide basis.

Loss event database (LED)

LED refers to a centralized database aimed at capturing information about operational losses. The losses tracked are mapped to the entities identified in the RCSA process.

Information such as the frequency, severity and nature of operational losses are captured. This data capture will allow analysis at the business segment and enterprise level. This will lead to a better understanding of the root causes of operational losses and improved risk mitigation strategies.

Ongoing development

Research and development efforts in the areas of quantification methodologies and key risk indicators will continue as we strive to stay at the forefront of risk management best practices.

Financial priority: Balance sheet and capital management

Highlights

- Consumer loans up 5%
- Deposits up 4%
- Internally generated capital of \$1.6 billion
- Capital ratios strengthened further
- Common share repurchases of \$764 million
- Redeemed US\$200 million of Series I and \$150 million of Series E preferred shares
- Redeemed \$400 million and issued US\$400 million of subordinated debentures

Total assets were \$377 billion at October 31, 2002, up \$17.7 billion or 5% from October 31, 2001.

Compared to October 31, 2001, securities were up \$13.3 billion or 17% and cash resources up \$3.8 billion or 22%. The growth in securities partially reflected higher levels of activity in our global equity derivatives business, which holds long and short positions in equity securities.

Total loans were up \$1 billion or .1% from October 31, 2001, with the acquisition of Eagle Bancshares in July 2002, contributing \$1.1 billion in loans and the acquisition of the private banking business of Barclays in June 2002, contributing \$.6 billion in loans. Consumer loans (residential mortgage, personal and credit card loans) were up \$5.5 billion or 5%. Residential mortgages were up \$5.4 billion or 8% (net of \$3.7 billion of mortgage securitizations during the year) and personal loans were down \$.5 billion or 2%. Credit card balances increased \$.6 billion or 15%, largely reflecting the maturity of \$.4 billion of credit card securitization term notes during the year. Business and government loans were down \$5.4 billion or 8%, largely reflecting planned reductions in the Canadian and U.S. corporate loan portfolios to enhance the quality of the business loan portfolio.

The \$.5 billion increase in Other assets was largely driven by a \$3.0 billion increase in derivative-related amounts. This increase in derivative-related amounts was largely offset by a \$1.9 billion decrease in acceptances. Other – Other assets of \$11.1 billion includes \$805 million (US\$517 million) of receivables due from Cooperatieve Centrale Raiffeisen-Boerenleenbank B.A. (Rabobank), relating to a derivative contract that is the subject of litigation with Rabobank. While the outcome of any litigation cannot be predicted with certainty, we expect to recover this amount in its entirety and accordingly have not recorded any provision for loss (for further information see Note 18 on page 90A).

Total deposits were \$243 billion, up \$10.0 billion or 4% from October 31, 2001. Interest-bearing deposits were up \$8.2 billion and non-interest-bearing deposits up \$1.8 billion. Personal deposits were up \$.5 billion, business and government deposits were up \$12.4 billion or 12% and bank deposits were down \$2.9 billion or 12%. Further details on deposits are provided in Note 10 on page 82A.

The fair value of loans and deposits differs from the respective book value due to changes in the levels of interest rates and changes in credit status. The estimated fair value of loans due from clients exceeded book values by \$2.3 billion at October 31, 2002 and \$4.2 billion at October 31, 2001. The estimated fair value of deposits owed to clients exceeded book values by \$1.7 billion at October 31, 2002, and \$2.7 billion at October 31, 2001. The net of the fair value excess of loans due from clients and the fair value excess of deposits due to clients was \$.6 billion at October 31, 2002, as shown in Note 21 on page 94A of our consolidated financial statements. The estimated fair value of loans and deposits were in excess of book values largely due to a decline in interest rates.

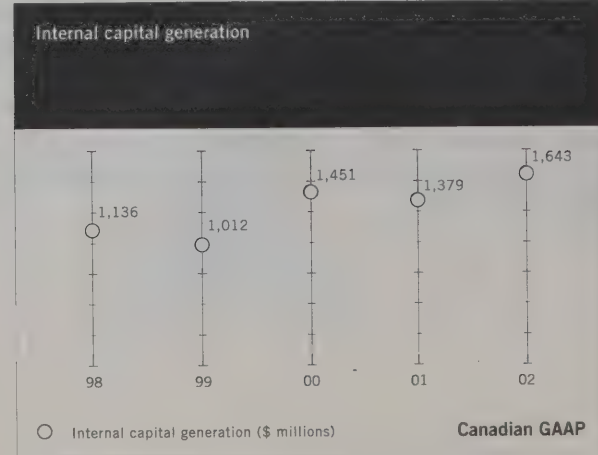
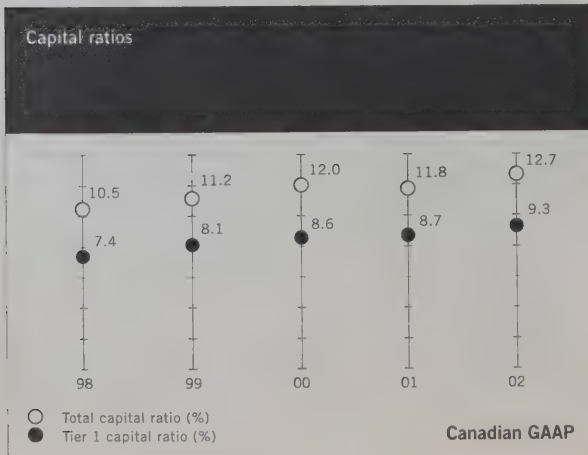
RBC Capital Trust, a closed-end trust, has a total of \$1.4 billion of transferable trust units (RBC TruCS) outstanding. RBC TruCS are reported as non-controlling interest in subsidiaries on the consolidated balance sheet and are included in Tier 1 capital under guidelines issued by OSFI.

Total balance sheet capital, which includes shareholders' equity and subordinated debentures, was \$25.4 billion at October 31, 2002, up \$.7 billion or 3% from a year ago. The most significant factor behind the increase in capital over 2001 was internal capital generation of \$1.6 billion, partially offset by net capital redemptions and net share repurchases of \$.9 billion during 2002.

We fund the pension plans in accordance with regulatory requirements, which generally require funding when there is a deficit on a funding basis. Different assumptions and methods are prescribed for regulatory funding purposes versus accounting purposes. Our pension plans are in a surplus position for regulatory funding purposes. Note 15 on page 87A describes the funding position for accounting purposes.

Capital management

Capital management requires balancing the desire to maintain strong capital ratios and high debt ratings with the need to provide competitive returns to shareholders. In striving for this balance, we consider expected levels of risk-adjusted assets and balance sheet assets, future investment plans and the costs and terms of current and potential capital issues.



We are committed to maintaining strong capital ratios through internal capital generation, the issuance of capital instruments when appropriate, and controlled growth in risk-adjusted assets. We were able to achieve strong levels of internal capital generation despite weaker capital market conditions during the past year. The market environment and planned reductions of corporate loan exposures also contributed to slower growth in risk-adjusted assets, enabling us to continue repurchasing shares and redeeming some of our outstanding capital instruments. Our debt ratings continue to enhance our ability to raise capital at competitive prices.

Capital management activity

In fiscal 2002, we repurchased 14.3 million common shares, of which 4.5 million shares were repurchased for \$229 million under a normal course issuer bid that expired in June 2002, and 9.8 million shares were repurchased for \$513 million under a normal course issuer bid that allows for the repurchase of up to 20 million common shares, representing approximately 3% of outstanding common shares, between June 24, 2002 and June 23, 2003. During the fourth quarter of 2001, we entered into an agreement with an independent third party to execute an accelerated repurchase of six million common shares. This agreement resulted in an additional repurchase cost of \$22 million this year. In total, we spent \$764 million in connection with our share repurchases during 2002.

In November 2001, we redeemed US\$200 million of First Preferred Shares Series I and, in October 2002, redeemed \$150 million of First Preferred Shares Series E.

In November 2001, we issued US\$400 million of subordinated debentures through our European Medium Term Note Programme. In September 2002, we redeemed \$400 million of subordinated debentures.

Regulatory capital

Capital levels for Canadian banks are regulated pursuant to guidelines issued by OSFI, based on standards issued by the Bank for International Settlements (BIS). Regulatory capital is allocated into two tiers. Tier 1 capital comprises the more permanent components of capital. The components of Tier 1 and Tier 2 capital are shown in Table 24 below.

Regulatory capital ratios are calculated by dividing Tier 1 and Total capital by risk-adjusted assets based on Canadian GAAP financial information. Risk-adjusted assets, as shown in Table 25 on page 60A, are determined by applying OSFI prescribed risk weights to balance sheet assets and off-balance sheet financial instruments according to the credit risk of the counterparty. Risk-adjusted assets also include an amount for the market risk exposure associated with our trading portfolio.

Our policy is to remain well capitalized so as to provide a safety net for the variety of risks to which we are exposed to in the conduct of our business. In 1999, OSFI formally established risk-based capital targets for deposit-taking institutions in Canada. These targets are a Tier 1 capital ratio of 7% and a Total capital ratio of 10%. As at October 31, 2002, our Tier 1 and Total capital ratios were 9.3% and 12.7%, respectively, compared to 8.7% and 11.8% at October 31, 2001. We maintained capital ratios that exceeded our medium-term goals of 8.0% for the Tier 1 ratio and 11–12% for the Total capital ratio. Effective November 1, 2002, we have raised our medium-term Tier 1 capital ratio goal to 8–8.5% from 8%. Our capital ratios on a U.S. basis, calculated using guidelines issued to U.S. banks by the Board of Governors of the Federal Reserve System and using U.S. GAAP financial information, are provided in Table 24 below.

Pending developments

In 1999, BIS issued a proposal for a new capital adequacy framework to replace the previous Capital Accord of 1988, under which we are currently regulated. This proposal continues to be at the discussion phase. Implementation of the final proposal is not likely to occur prior to fiscal 2006.

TABLE 24 Capital ratios (1)

(\$ millions, except percentage amounts)

| | 2002 | 2001 | 2000 |
|--|-------------------|-------------------|-------------------|
| Tier 1 capital | | | |
| Common equity | \$ 17,238 | \$ 16,141 | \$ 11,504 |
| Non-cumulative preferred shares | 1,545 | 2,024 | 2,037 |
| Non-controlling interest in subsidiaries | | | |
| RBC TruCS | 1,400 | 1,400 | 650 |
| Other | 29 | 28 | 23 |
| Goodwill | (4,832) | (4,742) | (647) |
| | 15,380 | 14,851 | 13,567 |
| Tier 2 capital | | | |
| Permanent subordinated debentures | 467 | 477 | 457 |
| Other subordinated debentures (2) | 6,147 | 5,935 | 5,138 |
| General allowance (3) | 1,420 | 1,410 | 1,188 |
| Non-controlling interest in subsidiaries | — | — | 1 |
| | 8,034 | 7,822 | 6,784 |
| Investment in insurance subsidiaries | (2,014) | (2,107) | (960) |
| Other substantial investments | (368) | (387) | (342) |
| First loss facility | (20) | (8) | (5) |
| Total capital | \$ 21,012 | \$ 20,171 | \$ 19,044 |
| Risk-adjusted assets | \$ 165,559 | \$ 171,047 | \$ 158,364 |
| Capital ratios (4) | | | |
| Common equity to risk-adjusted assets | 10.4% | 9.4% | 7.3% |
| Tier 1 capital to risk-adjusted assets | 9.3% | 8.7% | 8.6% |
| Total capital to risk-adjusted assets | 12.7% | 11.8% | 12.0% |
| Assets-to-capital multiple (5) | 17.3 | 17.2 | 15.3 |
| U.S. basis (4), (6) | | | |
| Tier 1 capital to risk-adjusted assets | 8.5% | 8.1% | 7.8% |
| Total capital to risk-adjusted assets | 11.9% | 11.2% | 11.3% |
| Equity to assets (7) | 4.9% | 5.3% | 4.5% |

(1) Using guidelines issued by the Superintendent of Financial Institutions Canada and Canadian GAAP financial information except as noted in footnote (6).

(2) Subordinated debentures that are within five years of maturity are subject to straight-line amortization to zero during their remaining term and, accordingly, are included above at their amortized value.

(3) The general allowance for credit losses may be included in Tier 2 capital up to a maximum of .875% (2000 and 1999 – .75%) of risk-adjusted assets. On October 27, 2000, we entered into a five-year agreement with a AAA rated reinsurer, which requires the reinsurer to purchase up to \$200 million of non-cumulative first preferred shares at the October 27, 2000 market price should the general allowance for credit losses be drawn down below a certain level. If these shares had been issued they would have qualified as Tier 1 capital.

(4) On November 26, 2001, we redeemed US\$200 million of Non-cumulative First Preferred Shares Series I, which reduced Tier 1 capital by the same amount. On November 8, 2001, we issued US\$400 million of subordinated debentures, which increased Total capital by the same amount. Had these transactions taken place as at October 31, 2001, the 2001 pro forma capital ratios would have been: Tier 1 capital ratio – 8.5% and Total capital ratio – 12.0%. Using guidelines issued by the Board of Governors of the Federal Reserve System in the United States and U.S. GAAP financial information, the pro forma U.S. basis capital ratios would have been Tier 1 capital ratio – 7.9% and Total capital ratio – 11.4%.

(5) Total assets and specified off-balance sheet financial instruments, as prescribed by the Superintendent of Financial Institutions Canada, divided by Total capital.

(6) Using guidelines issued by the Board of Governors of the Federal Reserve System in the United States and U.S. GAAP financial information.

(7) Average total shareholders' equity divided by average total assets.

| | Risk-adjusted assets (1) |
|------------------------------------|--------------------------|
| Assets subject to credit risk | 80,769 |
| Assets subject to market risk | 1,000 |
| Assets subject to operational risk | 1,000 |
| Total risk-adjusted assets | 81,769 |
| Capital resources | 10,000 |
| Capital adequacy ratio (%) | 12.23 |

| | | | Risk-adjusted balance | | | |
|--|-----------------|-------------------------------------|------------------------------|------------|------------|------------|
| | | | 2002 | 2001 | | |
| (\$ millions, except percentage amounts) | | | | | | |
| Balance sheet assets | | | | | | |
| Cash resources | \$ | 21,323 | 11% | \$ 2,284 | \$ 1,515 | |
| Securities | | | | | | |
| Issued or guaranteed by Canadian or other OECD governments | | 27,712 | 0% | 36 | — | |
| Other | | 66,088 | 11% | 7,137 | 7,341 | |
| Residential mortgages (3) | | | | | | |
| Insured | | 33,849 | 1% | 379 | 383 | |
| Conventional | | 38,950 | 52% | 20,168 | 18,511 | |
| Other loans and acceptances (3) | | | | | | |
| Issued or guaranteed by Canadian or other OECD governments | | 18,448 | 17% | 3,098 | 1,810 | |
| Other | | 121,893 | 74% | 89,836 | 97,553 | |
| Other assets | | 48,693 | 12% | 5,692 | 6,114 | |
| | | | \$ 376,956 | \$ 128,630 | \$ 133,227 | |
| | | | | | | |
| | Contract amount | Credit conversion factor | Credit equivalent amount | | | |
| Off-balance sheet financial instruments | | | | | | |
| Credit instruments | | | | | | |
| Guarantees and standby letters of credit | | | | | | |
| Financial | \$ 10,393 | 100% | \$ 10,393 | 82% | \$ 8,560 | \$ 8,629 |
| Non-financial | 3,217 | 50% | 1,609 | 100% | 1,609 | 1,422 |
| Documentary and commercial letters of credit | 772 | 20% | 154 | 97% | 150 | 148 |
| Securities lending | 23,967 | 100% | 23,967 | 3% | 646 | 393 |
| Commitments to extend credit | | | | | | |
| Original term to maturity of 1 year or less | 40,931 | 0% | — | — | — | — |
| Original term to maturity of more than 1 year | 34,115 | 50% | 17,058 | 92% | 15,638 | 18,821 |
| Uncommitted amounts | 45,978 | 0% | — | — | — | — |
| Note issuance/revolving underwriting facilities | 23 | 50% | 12 | 100% | 12 | 66 |
| | \$ 159,396 | | \$ 53,193 | | \$ 26,615 | \$ 29,479 |
| | | | | | | |
| | Notional amount | Gross positive replacement cost (4) | Credit equivalent amount (5) | | | |
| Derivatives | | | | | | |
| Interest rate contracts | | | | | | |
| Forward rate agreements | \$ 198,845 | \$ 178 | \$ 299 | 21% | \$ 64 | \$ 114 |
| Swaps | 862,264 | 19,608 | 24,357 | 26% | 6,323 | 5,617 |
| Options purchased | 55,293 | 563 | 914 | 28% | 258 | 123 |
| | 1,116,402 | 20,349 | 25,570 | | 6,645 | 5,854 |
| Foreign exchange contracts | | | | | | |
| Forward contracts | 544,719 | 6,802 | 13,049 | 28% | 3,685 | 3,881 |
| Swaps | 84,055 | 1,781 | 6,341 | 23% | 1,445 | 1,261 |
| Options purchased | 56,204 | 809 | 1,491 | 29% | 439 | 441 |
| | 684,978 | 9,392 | 20,881 | | 5,569 | 5,583 |
| Credit derivatives (6) | 52,151 | 861 | 2,963 | 29% | 858 | 369 |
| Other contracts (7) | 13,126 | 849 | 1,701 | 31% | 529 | 617 |
| Total derivatives before netting | \$ 1,866,657 | 31,451 | 51,115 | | 13,601 | 12,423 |
| Impact of master netting agreements | | (20,861) | (26,930) | | (7,132) | (6,339) |
| Total derivatives after netting | | \$ 10,590 | 24,185 | | 6,469 | 6,084 |
| Total off-balance sheet financial instruments | | \$ 77,378 | | | \$ 33,084 | \$ 35,563 |
| | | | | | 3,845 | 2,257 |
| General market risk | | | | | \$ 165,559 | \$ 171,047 |
| Total risk-adjusted assets | | | | | | |

- (1) Using guidelines issued by the Superintendent of Financial Institutions Canada and Canadian GAAP financial information.
- (2) Represents the weighted average of counterparty risk weights within a particular category.
- (3) Amounts are shown net of allowance for loan losses.
- (4) Represents the total current replacement value of all outstanding contracts in a gain position, before factoring in the impact of master netting agreements. Exchange-traded instruments are subject to daily margin requirements. Such instruments are excluded from the calculation of risk-adjusted assets as they are deemed to have no additional credit risk. The fair value of \$194 million (2001 – \$194 million) is excluded at October 31, 2002. Written options are excluded as they represent our obligations and as such do not attract credit risk.
- (5) Consists of (i) the total positive replacement value of all outstanding contracts, and (ii) an amount for potential future credit exposure.
- (6) Comprises credit default swaps, total return swaps and credit default baskets.
- (7) Comprises precious metals, commodity and equity-linked derivative contracts.

Asset/liability management

Overview

Asset/liability management comprises the evaluation, monitoring and management of our non-trading portfolio, liquidity management and funding. It is important to note that liquidity and capital resources are likely to be affected by many of the same factors which are detailed in this section of Management's discussion and analysis, the Factors discussion on pages 23A to 24A and the Risk management discussion on pages 53A to 57A. Additionally, off-balance sheet financing arrangements are often integral to both liquidity and capital resources, and are discussed in detail on pages 64A to 65A of this section.

Non-trading portfolio

Traditional banking activities, such as deposit taking and lending, expose us to market risk, of which interest rate risk, as described on page 55A, is the largest component.

We actively manage the interest rate risk for the North American non-trading balance sheet and oversee all other non-trading units that have been delegated interest rate risk limits. We endeavour to adopt industry best practices and carry out the following functions:

Policy

The Conduct Review and Risk Policy Committee of the Board of Directors approves the global policies governing interest rate risk management. The policies define the acceptable limits within which risks to net interest income over a 12-month horizon and the economic value of equity are to be managed. These ranges are based on immediate and sustained \pm 200 basis points parallel shifts of the yield curve. The limit for net interest income risk is 6% of projected net interest income and for economic value of equity risk is 12% of projected common equity.

Interest rate funds transfer pricing

We use a funds transfer pricing mechanism to centralize interest rate risk within Corporate Treasury and to ensure an economic allocation of interest income to the various business units. Funds transfer pricing at the transaction level ensures that interest rate risk is appropriately transferred to Corporate Treasury for management. The funds transfer pricing rates are market-based and aligned with risk management principles. They are supported by empirical research into client behaviour and are an integral input to the retail business pricing decisions.

Applied research

We are dedicated to investigating best practices in instrument valuation, econometric modeling and new hedging techniques. These investigations range from evaluation of traditional asset/liability management processes to application of recent developments in quantitative methods to our processes.

We focus on developing retail product valuation models that incorporate consumer behaviour. These valuation models are typically derived through econometric estimation of consumer exercise of options embedded in retail products. The most significant embedded options are mortgage rate commitments and prepayment options. On the liability side of the balance sheet, we tend to focus on modeling administered rates and the sensitivity of liability balances to interest rate changes.

Risk measurement

We continue to make significant investment in new technology to facilitate measurement and timely management of our interest rate risk position. A range of static and dynamic scenarios is used every week to measure our risk position based on client rates as well as funds transfer pricing rates.

Static scenarios allow us to analyze our risk at a particular point in time under various interest rate assumptions. These assumptions comprise parallel shocks as well as twists to the current yield curve. Static scenarios are employed for assessing the economic value of equity risk as well as the net interest income risk. Dynamic scenarios simulate our interest income in response to various combinations of business and market factors. Business factors include assumptions about future pricing strategies and volume and mix of new business, whereas market factors include assumptions such as changes in interest rate levels and changes in the shapes of yield curves.

We measure our risk positions for the Canadian non-trading balance sheet every week and are capable of identifying the various sources of interest rate risk.

Interest rate risk management

Our goal is to manage interest rate risk of the non-trading balance sheet to a targeted level, on a continual basis. We modify the risk profile of the balance sheet through proactive hedging activity.

The interest rate risk can be disaggregated into linear risk and non-linear risk based on the varying responses of the balance sheet to different interest rate movements. The linear risk is primarily managed through interest rate swaps. The non-linear risk arises mainly from embedded options in our products that allow clients to modify the maturities of their loans or deposits. Examples are a client pre-paying a personal loan or a prospective client getting a committed rate on a new mortgage before the mortgage loan takes effect. Embedded options are modeled using assumptions based on empirical research and are managed by either purchasing options or by a dynamic hedging strategy.

The performance of interest rate risk management function within Corporate Treasury is benchmarked on a total return basis. A by-product of this benchmarking exercise is a methodology that controls model risk by continuously back-testing model assumptions against actual client behaviour.

Table 26 below presents the potential impacts of 100 and 200 basis point increases and decreases in interest rates on our economic value of equity and on current earnings on our non-trading portfolio. These measures are as of October 31, 2002, and are based on assumptions made by management and validated by empirical research. The methodology assumes that no further hedging is undertaken. We have defined a risk neutral balance sheet as one where net residual assets representing equity are evenly invested over a five-year horizon. As a result of this decision, our interest rate risk profile has slightly faster re-pricing of assets than of liabilities with the duration of equity at about 2.5 years.

All interest rate measures in this section are based upon our interest rate exposures at a specific time. The exposures change continually as a result of day-to-day business activities and our risk management initiatives.

TABLE 26 Market risk measures – Non-trading activities ⁽¹⁾

| (\$ millions) | 2002 | | 2001 | |
|----------------|-------------------------------|--------------------------|-------------------------------|--------------------------|
| | Economic value of equity risk | Net interest income risk | Economic value of equity risk | Net interest income risk |
| 100bp increase | \$ (309) | \$ 104 | \$ (390) | \$ 96 |
| 100bp decrease | 145 | (151) | 256 | (108) |
| 200bp increase | \$ (662) | \$ 190 | \$ (842) | \$ 179 |
| 200bp decrease | 345 | (327) | 466 | (294) |

(1) Amounts are presented on a pre-tax basis as at October 31.

Liquidity management

Our liquidity management framework is designed to ensure that reliable and cost-effective sources of cash are available to satisfy current and prospective commitments, both on and off-balance sheet. The primary goals of this framework are the preservation of a large base of core client deposits, ongoing access to diversified sources of wholesale funding and the maintenance of a dedicated pool of unencumbered marketable securities that provide ready access to cash.

The Corporate Treasury function has global responsibility for the development of liquidity management policies, strategies and contingency plans and for recommending and monitoring limits within this framework. Our principal regional trading and funding platforms provide transactional support for liquidity management policies and strategies. The Group Risk Management Committee and the Asset/Liability Committee share management oversight of liquidity management and receive regular reports detailing compliance with limits and guidelines. The Audit Committee of the Board of Directors approves our liquidity management framework and significant related policies and is informed on a periodic basis about our current and prospective liquidity condition. Additionally, we have a liquidity contingency plan in place, which is maintained and administered by the Liquidity Crisis Team. Subsidiaries are responsible for managing their own liquidity in compliance with policies, practices and governing regulatory requirements.

We measure and monitor our liquidity condition from structural, tactical and contingent perspectives. The assessment of our liquidity position based on these measures reflects management estimates and judgments pertaining to the behaviour of our clients and future market conditions.

Structural liquidity risk management

Existing balance sheet composition can create liquidity exposure due to mismatches in effective maturities between assets and liabilities. Structural liquidity risk management addresses this type of exposure, which is measured and monitored through ongoing stress testing of our balance sheet.

We recently adopted the cash capital model to assist in the evaluation of balance sheet liquidity and in the determination of the appropriate term structure of our debt financing. This methodology provides a comprehensive, formula-based approach for the assessment of balance sheet integrity and our ability to continue as a going concern during a prolonged liquidity event, such as an unexpected withdrawal of short-term funding. The application of this model entails assigning liquidity discounts or "haircuts" to our balance sheet assets based on our assessment of the cash-generating characteristics of each asset category in the context of a sustainable business model. The illiquid component of our balance sheet assets can be determined by this analysis. Liabilities are arrayed along a stability continuum, ranging from core to volatile, on the basis of both contractual and behavioural properties in order to identify the constant elements of our funding. This analysis of our balance sheet enables us to more accurately estimate our exposure to a protracted loss of unsecured funding and to quantify our longer-term financing requirements.

Tactical liquidity risk management

Tactical liquidity risk management addresses our normal day-to-day funding requirements and is managed by imposing limits on net funds outflows for specified periods, particularly for key short-term time horizons. Scenario analysis is performed periodically on the assumed behaviour of cash flows under varying conditions to assess funding requirements and, as required, to update assumptions and limits. Detailed reports on our principal short-term asset/liability mismatches are monitored on a daily basis to ensure compliance with the prudential limits established for overall group exposure and by major currency and geographic location. Corporate Treasury issues procedural directives to the individual units engaged in executing policy to ensure consistent application of cash flow management principles across the entire organization.

Contingent liquidity risk management

The liquidity contingency plan identifies comprehensive action plans that would be implemented in the event of general market disruptions or adverse economic developments that could jeopardize our ability to meet commitments. Four different market scenarios, of varying duration and severity, are addressed in the liquidity contingency plan to highlight potential liquidity exposures and requisite responses. The Liquidity Crisis Team, comprising senior individuals from business and functional units, meets regularly to review and update implementation plans and to consider the need for activation in view of developments in Canada and globally.

To address potential liquidity exposures identified by our scenario analyses, we maintain a pool of segregated and unencumbered marketable securities. These high-quality assets can be readily sold or pledged for secured borrowing and represent a dedicated and reliable source of emergency funding. In addition, we maintain a separate portfolio of eligible assets to support our participation in Canadian payment and settlement systems. Liquid assets and assets purchased under reverse repurchase agreements (before pledging as detailed below) totalled \$154 billion or 41% of total assets at October 31, 2002, as compared to \$136 billion or 38% respectively at October 31, 2001. Canadian dollar liquid assets are primarily marketable securities while a material portion of our foreign currency liquid assets are issued by highly rated foreign banks. As at October 31, 2002, \$10 billion of assets had been pledged as collateral, unchanged from October 31, 2001. We have another \$40 billion in obligations related to assets sold under repurchase agreements or securities sold short at October 31, 2002, compared to \$37 billion at October 31, 2001. For further details, see Note 18 on page 91A.

Funding strategy

Diversification of funding sources is a crucial component of our overall liquidity management strategy since it expands funding flexibility, minimizes funding concentration and dependency and generally lowers financing costs. Core funding, comprising capital, longer-term liabilities and a diversified pool of personal and, to a lesser extent, commercial deposits, is the foundation of our strong structural liquidity position.

Credit ratings

Our ability to access unsecured funding markets and our financing costs in such markets are primarily dependent upon maintaining acceptable credit ratings, which in turn is largely determined by the quality of our earnings, the adequacy of our capital and the effectiveness of our risk management programs. While our estimates suggest that a minor downgrade would not materially influence our funding capacity or costs, we recognize the importance of avoiding such an event and are committed to actions that should reinforce existing external assessments of the bank's financial strength. A series of downgrades could have an adverse impact on our funding capacity and on the results of our operations.

Deposit profile

Personal deposits remain the prime source of funding for our Canadian dollar balance sheet while most foreign currency deposits originate from unsecured, "wholesale" sources, including large corporate and institutional clients and foreign commercial and central banks. Our personal deposit franchise constitutes a principal source of predictable and dependable funding. Certain commercial and institutional client groups also maintain relational balances with relatively low volatility profiles, a portion of which are considered core funding for structural liquidity purposes. Relational balances are typically maintained by commercial and corporate clients to facilitate their daily operating requirements. In some businesses, collective balances are substantial and exhibit a high degree of relative stability. We promote wholesale funding diversity and regularly review sources of short-term funds to ensure maintenance of wide

diversification by provider, product and geographic origin. In addition, we maintain an ongoing presence in different funding markets, constantly monitoring market developments and trends in order to identify opportunities or risks and to take appropriate pre-emptive actions. For further details see Note 10 on page 83A.

Term funding sources

Long-term funding strategy is integrated with our current and estimated structural liquidity position as reflected in our cash capital position. Liquidity objectives, as well as market conditions, interest rates, credit spreads and desired financial structure, influence annual long-term funding activities, including currency mix and market concentration. Diversification into new markets and untapped investor segments is constantly evaluated against relative issuance costs. Our long-term funding sources are managed to minimize concentration by geographic location, investor segment, and currency and maturity profile. During fiscal 2002, we continued to expand our long-term funding base by issuing \$2.6 billion of senior deposit notes in various currencies and markets. Total unsecured long-term funding outstanding at October 31, 2002, was \$13.2 billion, compared with \$12.6 billion at October 31, 2001.

We use asset securitization programs as an alternative source of funding, to provide liquidity and for asset/liability management purposes. In particular, \$1.7 billion in new financing was provided during the year by the securitization and sale of government guaranteed residential mortgages (MBS). Our total outstanding MBS sold at year-end was \$2.4 billion. In addition, \$1.7 billion of our credit card receivables have been securitized through notes issued by a securitization SPE (see page 64A, Special purpose entities – securitization for more details).

Off-balance sheet

In the normal course of business, we engage in a variety of financial transactions that, under GAAP, are either not recorded on our balance sheet or are recorded on our balance sheet in amounts that differ from the full contract or notional amounts. These transactions involve, among other risks, varying degrees of market, credit and liquidity risk, which are discussed in the Risk management section on pages 53A to 57A. Off-balance sheet transactions are either proprietary or client transactions, and are generally undertaken for risk management, capital management and/or funding management purposes. The types of off-balance sheet activities we undertake include issuance of credit instruments and lease commitments, derivative financial instruments and transactions with SPEs. Each of these types of activities is discussed below.

Credit instruments

We provide credit instruments to our clients to help them meet their financing needs. Guarantees and standby letters of credit carry the same credit risk as loans and represent irrevocable assurances that we will make payments in the event that a client cannot meet its obligations to

third parties. On behalf of clients, we also undertake written documentary and commercial letters of credit, authorizing a third party to draw drafts from us to a stipulated amount and typically having underlying shipments of goods as collateral. We make commitments to extend credit, which may represent unused portions of authorizations to extend credit in the form of loans, acceptances, guarantees and letters of credit. We have uncommitted amounts, which represent revocable offers by us to extend credit to a borrower, but not obligations to extend credit. We are also party to note issuance facilities (including revolving facilities), which represent underwriting agreements that enable a borrower to issue short-term debt securities. Table 27 below provides a detailed summary of our off-balance sheet credit instruments.

Lease commitments

We have made minimum future rental commitments for premises and equipment under long-term non-cancellable leases, which are detailed for each of the next five years and thereafter in Table 27 below. Our lease agreements do not contain any covenants that restrict our ability to pay dividends, engage in debt or equity financing transactions, or enter into additional lease agreements.

Derivative financial instruments

As a part of our institutional sales and trading activities, we act as counterparty to clients in transactions involving derivative financial instruments. We undertake this role to assist our clients in managing their exposure to various types of risk. We also engage in transactions involving derivative financial instruments with other counterparties to manage our exposure to interest rate, currency, credit and market risks (market risks are discussed on page 55A). All derivatives, except those for other than trading purposes, are recorded at fair value on our balance sheet (fair value assumptions are discussed on page 25A). Although derivative transactions are measured in terms of their notional amounts, these amounts are not recorded on our balance sheet, as the notional amounts serve as points of reference for calculating payments, and are not the actual amounts that are exchanged. Table 25 on page 60A details the notional amount, credit equivalent amount and risk-adjusted balances by derivative contract type. The table in Note 19 on pages 92A and 93A, details the notional amount of derivatives by reference to term to maturity and replacement cost, respectively.

To the extent that one or more of the derivative financial transactions we undertake involve amounts owing from third-party counterparties, we are exposed to counterparty credit risk (credit risk is discussed in more detail on page 54A). Total credit risk as represented by the fair value of all derivatives that have a positive market value amounted to \$10.6 billion as at October 31, 2002, and is recorded at replacement cost on our balance sheet. Additionally, Notes 1 and 19 on pages 73A and 91A to 93A, respectively, provide more detail on the accounting for derivatives.

TABLE 27 Lease commitments and credit instruments

| (\$ millions) | Within 1 year | 1 to 3 years | Over 3 to 5 years | Over 5 years | Total |
|--|---------------|--------------|-------------------|--------------|------------|
| Lease commitments | \$ 364 | \$ 630 | \$ 470 | \$ 754 | \$ 2,218 |
| Credit instruments | | | | | |
| Guarantees and standby letters of credit | 4,159 | 6,247 | 1,526 | 1,678 | 13,610 |
| Documentary and commercial letters of credit | 378 | 236 | 118 | 40 | 772 |
| Commitments to extend credit | 44,832 | 10,624 | 4,233 | 15,357 | 75,046 |
| Uncommitted amounts | 814 | 41,121 | 2,835 | 1,208 | 45,978 |
| | 50,183 | 58,228 | 8,712 | 18,283 | 135,406 |
| Total | \$ 50,547 | \$ 58,858 | \$ 9,182 | \$ 19,037 | \$ 137,624 |

Special purpose entities

Special purpose entities (SPEs) are principally used to securitize financial and other assets in order to obtain access to funding, to mitigate credit risk and to manage capital. SPEs are an important part of the financial markets, providing market liquidity by facilitating investors' access to specific portfolios of assets and risks in a form that meets their investment criteria. We use SPEs to securitize a portion of our credit card receivables. We provide SPE repackaging services to clients who seek access to financial assets in a form different than what is conventionally available. We also act as an intermediary or agent for clients who want to use SPEs to securitize their own financial assets.

SPEs are typically set up for a single, discrete purpose, have a limited life and serve to legally isolate the financial assets held by the SPE from the selling organization. SPEs are not operating entities and usually have no employees. The typical SPE structure involves a company selling assets to the SPE. The SPE funds the purchase of those assets by issuing securities to investors in the form of certificates, commercial paper or other notes of indebtedness. The financial interests of investors in SPEs are usually limited to interests in the assets of the SPE, and to various forms of credit enhancement accompanying the SPE assets, which may include conditional access to a cash collateral account, over-collateralization in the form of excess assets in the SPE or a line of credit facility. Liquidity and credit facilities as well as interest rate and other swaps may be provided by financial institutions to address mismatches between the cash flows of the underlying assets and the indebtedness issued by the SPE.

We provide services to SPEs in a number of different capacities including administration of the SPEs and the underlying asset pools, as a trustee for SPEs' assets, as a liquidity or credit enhancement provider, or as a counterparty in transactions involving derivative financial instruments or as collateral manager.

We manage and monitor our direct involvement with SPEs through our SPE Risk Committee, which comprises representatives from functional areas including risk management, corporate treasury, finance, subsidiary governance office, law, taxation, subsidiary banking groups and human resources. This committee's key activities include formulating policies governing SPEs, reviewing new and unusual SPE transactions and monitoring the ongoing activities of SPEs.

The CICA is currently drafting new accounting standards on the consolidation of SPEs. Since these new standards are still being drafted their impact on our balance sheet is not quantifiable but could result in us consolidating certain assets and liabilities held in our SPEs.

Securitization of credit card receivables

We securitize some of our credit card receivables through an SPE. The SPE is funded through the issuance of senior and subordinated notes collateralized by the underlying credit card receivables. The primary economic purpose of this activity is to diversify our sources of funding and to enhance our liquidity position. Although these credit card receivables are no longer on our balance sheet, we maintain the client account and retain the relationship.

The transfer of the credit card receivables to the custodian of those assets is a sale from a legal perspective. In addition, our credit card securitization structure qualifies for sale treatment from an accounting perspective. Under AcG-12, the receivables are removed from our balance sheet resulting in a gain or loss reported in other income. Note 7 on page 81A provides information on our key securitization activities, including key assumptions. This SPE meets the AcG-12 criteria for a Qualifying SPE (QSPE) and, accordingly, as the transferor of the credit card receivables, we are precluded from consolidating this SPE.

We continue to service the credit card receivables sold to the QSPE. In addition, we perform an administrative role for the QSPE in which we are responsible for ensuring that the ongoing public filings of the QSPE are performed, as required, and that the investors in the QSPE's asset-backed securities receive interest and principal payments on a timely basis.

We provide first loss protection to the QSPE in two forms. Our interest in the excess spread from the QSPE is subordinate to the QSPE's obligation to the holders of its asset-backed securities. Excess spread is the residual net interest income after all other trust expenses have been paid. Therefore, our excess spread serves to absorb losses with respect to the credit card receivables before payments to the QSPE's noteholders are affected. Under AcG-12, the present value of excess spread of credit card receivables sold on or after April 1, 2001, is reported as a retained interest within investment account securities on our consolidated balance sheet. Whereas, the excess spread of credit receivables sold prior to April 1, 2001, is recognized in other income when received from the QSPE. In addition, we provide loans to the QSPE to pay up-front expenses. These loans rank subordinate to all notes issued by the QSPE.

At October 31, 2002, total credit card receivables securitized and held off-balance sheet amounted to \$1.7 billion, compared to \$2.1 billion at October 31, 2001. The carrying value of our retained interests held in securitized credit card receivables at October 31, 2002, was \$9.1 million compared to \$9.5 million in 2001, and amounts receivable under subordinated loan agreements were \$5.2 million compared to \$8.5 million in 2001.

Securitization of client financial assets

Within our global securitization group, our principal relationship with SPEs comes in the form of administering multi-seller asset-backed commercial paper conduit programs (multi-seller SPEs). We currently administer five multi-seller SPEs – three in Canada and two in the U.S. These five multi-seller SPEs have purchased financial assets from our clients totalling \$20.6 billion. Under current accounting standards, the five multi-seller SPEs that we administer are not consolidated on our balance sheet.

We are involved in the multi-seller SPE markets because our clients value these transactions, they offer a growing source of revenue and they generate a favorable risk-adjusted return for us. Our clients primarily utilize multi-seller SPEs to diversify their financing sources and to reduce funding costs by leveraging the value of high-quality collateral.

The multi-seller SPEs purchase various financial assets from clients and finances those purchases by issuing highly rated asset-backed commercial paper. The multi-seller SPEs typically purchase the financial assets as part of a securitization transaction by our clients. In these situations, the sellers of the financial assets continue to service the respective assets and generally provide some amount of first-loss protection on the assets. We do not maintain any ownership or retained interest in these multi-seller SPEs. Instead, we provide or retain certain services such as transaction structuring and administration as specified by the multi-seller SPE's program documents and based on rating agency criteria. In addition, we provide backstop liquidity facilities and partial credit enhancement to the multi-seller SPEs. We receive market-based fee revenue from such services, which is reported as other income. We also have no rights to, or control of, the assets owned by the multi-seller SPE.

The table below summarizes the financial assets owned by the multi-seller SPEs at fiscal years ended October 31.

| Asset class | | | |
|-------------------------------|------------------|-----------|---------------|
| (\$ millions) | | | |
| | 2002 | | 2001 |
| Credit cards | \$ 4,671 | \$ | 3,785 |
| Auto loans and leases | 3,615 | | 4,298 |
| Equipment receivables | 2,509 | | 2,159 |
| Trade receivables | 2,479 | | 2,094 |
| Residential mortgages | 2,004 | | 1,682 |
| Other loans | 1,275 | | 843 |
| Dealer floor plan receivables | 1,208 | | 1,275 |
| Consumer loans | 1,196 | | 1,114 |
| Asset-backed securities | 926 | | 487 |
| Other | 706 | | 579 |
| | \$ 20,589 | \$ | 18,316 |

The commercial paper issued by each multi-seller SPE is in the SPE's own name with recourse to the financial assets owned by the multi-seller SPE. The multi-seller SPE commercial paper is non-recourse to us and non-recourse to the other multi-seller SPEs that we administer. Each multi-seller SPE is largely prohibited from issuing medium-term notes or other forms of indebtedness to finance the asset purchases. Consequently, each multi-seller SPE's commercial paper liabilities are generally equal to the assets owned by that multi-seller SPE. The small difference between each of the multi-seller SPE's assets and liabilities balances is mostly related to the discount or interest costs attributable to the commercial paper. As of October 31, 2002, the total face amount of commercial paper issued by the multi-seller SPE's equaled \$20,589 million generating \$20,534 million of cash proceeds with the difference between these amounts representing the commercial paper discount.

At fiscal years ended October 31, total commitments and amounts outstanding under liquidity and credit facilities were as shown in the following table:

| Liquidity and credit facilities | | | | |
|--|------------------|-------------|------------------|-------------|
| | 2002 | | 2001 | |
| (\$ millions) | Committed | Outstanding | Committed | Outstanding |
| Liquidity facilities | \$ 22,593 | \$ – | \$ 20,614 | \$ – |
| Credit facilities | 7,211 | – | 3,856 | – |
| | \$ 29,804 | \$ – | \$ 24,470 | \$ – |

We provide backstop liquidity facilities to the multi-seller SPEs as an alternative source of financing in the event that such SPEs are unable to access commercial paper markets, or in limited circumstances, when pre-determined performance measures of the financial assets owned by the multi-seller SPEs are not met. The terms of the backstop liquidity facilities do not require us to advance money to the multi-seller SPEs in the event of bankruptcy or to purchase non-performing or defaulted assets. None of the backstop liquidity facilities that we have provided has ever been drawn upon.

The partial credit enhancement that we provide to the multi-seller SPEs is in place to protect commercial paper investors in the event that the credit enhancement supporting the asset pools proves to be insufficient to prevent a default of one or more of the asset pools. Each of the asset pools is structured to achieve a high investment grade credit profile through credit enhancement related to each transaction. As a result, we believe that the program credit enhancements that we provide to the multi-seller SPEs present a modest amount of credit risk.

The economic exposure that we assume when we provide backstop liquidity commitments and partial credit enhancement is contingent in

nature. We manage these exposures within our risk management functions in the same manner that we manage other contingent and non-contingent risk exposures. Our risk management process considers the credit, liquidity and interest rate exposure related to each of the assets. The risk exposure of each of these components individually and taken as a whole is deemed to be acceptable. All transactions are reviewed by external rating agencies. The weighted average credit quality of the assets supported by our backstop liquidity and partial credit enhancement is among the highest quality rating levels based on our internal risk rating system, which is described on page 54A. The liquidity risk to us is deemed to be low based on the historical performance and high credit quality of the multi-seller SPEs' assets. Interest rate exposure is deemed to be low and is generally managed at the transaction level by passing on the funding cost variability to the securitization structures. Corporate Treasury scrutinizes contingent balance sheet risk, in effect monitoring the risk of drawdown under any of the credit facilities.

Creation of investment products

We use repackaging SPEs to create unique credit products to meet the needs of investors with specific requirements. As part of this process, we may enter into derivative contracts with these SPEs in order to convert various risk factors such as yield, currency or credit risk of underlying assets to meet the needs of our clients. In this role as derivative counterparty to the SPE, we assume the associated counterparty credit risk of the SPE. In order to enter into these transactions we establish an internal risk rating of the SPE and provide ongoing risk assessment and monitoring of the SPE's credit risk. As with all counterparty credit exposures, these exposures are put in place and reviewed pursuant to our normal risk management process in order to effectively manage and monitor this credit risk profile.

These SPEs often issue notes. Those notes may also be rated by external rating agencies, as well as listed on a stock exchange and are generally traded via recognized bond clearing systems. While the majority of the notes that are created in repackagings are expected to be sold on a 'buy & hold' basis, we may on occasion act as market-maker. We do not, however, provide any repackaging SPE with any guarantees or other similar support commitments. There are many functions required to create a repackaged product. We fulfill some of these functions and independent third parties or specialist service providers fulfill the remainder. Currently we act as sole arranger and swap provider for SPEs where we are involved, and in most cases as paying and issuing agent as well.

Asset management

We act as collateral manager for several collateralized debt obligation (CDO) SPEs, which invest in leveraged bank-initiated term loans, high-yield bonds and mezzanine corporate debt. As collateral manager, we are engaged by the CDO SPE, pursuant to a Collateral Management Agreement, to advise the SPE on the purchase and sale of collateral assets it holds. For these advisory services, we are paid a pre-determined market-based fee, which is a percentage of assets held by the SPE.

The notional amount of the CDOs we managed at the end of fiscal 2002 was US\$1.6 billion (2001 – US\$1.3 billion). Although we have a nominal investment of US\$9.5 million in the "first-loss" tranche of a US\$300 million CDO, we provide no liquidity or credit support to these SPEs beyond this investment. The CDOs we manage may from time-to-time purchase collateral assets originated by us or other affiliates. The program documents covering the formation and operation of the individual CDOs provide strict guidelines for the purchase of such assets.

We recognize fee income from collateral management services and, where indicated, interest income from investments in individual CDOs.

2001 compared to 2000

The following discussion and analysis provides a comparison of our results of operations for the years ended October 31, 2001 and 2000. This discussion should be read in conjunction with the consolidated financial statements and related Notes on pages 67A to 97A. This portion of the management's discussion and analysis is based on amounts reported in the consolidated financial statements and does not exclude special items.

Business segment results

Net income from RBC Banking increased 10% to \$1,181 million in 2001 from \$1,078 million in 2000. ROE decreased 280 basis points to 16.9%.

Net income from RBC Insurance was up 1% to \$133 million in 2001, reflecting acquisitions. ROE decreased from 49% to 15% due to higher allocation of capital in light of recent acquisitions.

Net income from RBC Investments was up 23% from 2000 to \$513 million. ROE declined by 2,100 basis points to 27.2% due to higher allocation of capital as a result of recent acquisitions.

Net income from RBC Capital Markets decreased 34% to \$336 million, reflecting a large increase in the provision for credit losses. ROE declined by 1,180 basis points to 9.3%, reflecting lower net income and the higher allocation of capital for recent acquisitions.

Net income from RBC Global Services was up 42% to \$263 million reflecting the growth from new business and value-added services added in the investor services business. ROE increased 940 basis points to 48.9%.

Other segment's net income improved to \$(15) million from \$(45) million in 2000. ROE increased 10 basis points to (2.8)%.

Quarterly financial information

Selected financial information for the eight most recently completed quarters is shown on page 102A.

Net interest income

Net interest income increased 23% to \$6.5 billion in 2001 from \$5.3 billion in 2000 partially due to the acquisition of Centura Banks, in June 2001 which added more interest-bearing assets and liabilities to the balance sheet.

Other income

Other income increased 22% to \$8.2 billion in 2001, accounting for 56% of total revenue.

Non-interest expense

Non-interest expense increased 29% to \$9.8 billion, partially reflecting the contribution of expenses from acquisitions and an increase of goodwill amortization expenses associated with these acquisitions.

Taxes

Our income taxes for 2001 were \$1.3 billion, for an effective income tax rate of 34.7%. Income taxes were \$1.4 billion in 2000, reflecting an effective income tax rate was 38.6%.

Provision for credit losses

The provision for credit losses increased 62% to \$1,119 million in 2001 from \$691 million in 2000, largely reflecting increases in business and government provisions for credit losses. The total allowance for loan losses was \$2.3 billion or 1.1% of total loans, acceptances and reverse repurchase agreements up from 1.0% in 2000.

Consolidated financial statements

Management's responsibility for financial reporting

The accompanying consolidated financial statements of Royal Bank of Canada were prepared by management, which is responsible for the integrity and fairness of the information presented, including the many amounts that must of necessity be based on estimates and judgments. These consolidated financial statements were prepared in accordance with Canadian generally accepted accounting principles, including the accounting requirements of the Superintendent of Financial Institutions Canada. Financial information appearing throughout this Annual Report is consistent with these consolidated financial statements. Management has also prepared consolidated financial statements for Royal Bank of Canada in accordance with United States generally accepted accounting principles, and these consolidated financial statements have also been provided to shareholders.

In discharging its responsibility for the integrity and fairness of the consolidated financial statements and for the accounting systems from which they are derived, management maintains the necessary system of internal controls designed to ensure that transactions are authorized, assets are safeguarded and proper records are maintained. These controls include quality standards in hiring and training of employees, policies and procedures manuals, a corporate code of conduct and accountability for performance within appropriate and well-defined areas of responsibility.

The system of internal controls is further supported by a compliance function, which ensures that the bank and its employees comply with securities legislation and conflict of interest rules, and by an internal audit staff, which conducts periodic audits of all aspects of the bank's operations.

The Board of Directors oversees management's responsibilities for financial reporting through an Audit Committee, which is composed entirely of directors who are neither officers nor employees of the bank.

This Committee reviews the consolidated financial statements of the bank and recommends them to the board for approval. Other key responsibilities of the Audit Committee include reviewing the bank's existing internal control procedures and planned revisions to those procedures, and advising the directors on auditing matters and financial reporting issues. The bank's Compliance Officer and Chief Internal Auditor have full and unrestricted access to the Audit Committee.

At least once a year, the Superintendent of Financial Institutions Canada makes such examination and enquiry into the affairs of the bank as deemed necessary to ensure that the provisions of the *Bank Act*, having reference to the safety of the depositors and shareholders of the bank, are being duly observed and that the bank is in sound financial condition.

Deloitte & Touche LLP and PricewaterhouseCoopers LLP, independent auditors appointed by the shareholders of the bank upon the recommendation of the Audit Committee, have performed an independent audit of the consolidated financial statements and their report follows. The shareholders' auditors have full and unrestricted access to the Audit Committee to discuss their audit and related findings.

Gordon M. Nixon
President & Chief Executive Officer

Peter W. Currie
Vice-Chairman & Chief Financial Officer

Toronto, November 19, 2002

Auditors' report

To the shareholders of Royal Bank of Canada

We have audited the consolidated balance sheet of Royal Bank of Canada as at October 31, 2002 and 2001, and the consolidated statements of income, changes in shareholders' equity and cash flows for each of the years in the three-year period ended October 31, 2002. These consolidated financial statements are the responsibility of the bank's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the bank as at October 31, 2002 and 2001, and the results of its operations and its cash flows for each of the years in the three-year period ended October 31, 2002, in accordance with Canadian generally accepted accounting principles, including the accounting requirements of the Superintendent of Financial Institutions Canada.

We also reported separately on November 19, 2002, to the shareholders of the bank on our audit, conducted in accordance with Canadian generally accepted auditing standards, where we expressed an opinion without reservation on the October 31, 2002 and 2001, consolidated financial statements, prepared in accordance with United States generally accepted accounting principles.

Deloitte & Touche LLP
PricewaterhouseCoopers LLP
Chartered Accountants

Toronto, November 19, 2002

Consolidated balance sheet

| As at October 31 (\$ millions) | 2002 | 2001 |
|--|-------------------|------------|
| Assets | | |
| Cash resources | | |
| Cash and due from banks | \$ 2,534 | \$ 1,792 |
| Interest-bearing deposits with banks | 18,789 | 15,743 |
| | 21,323 | 17,535 |
| Securities | | |
| Trading account (pledged – \$6,558 and \$4,222) | 68,328 | 58,192 |
| Investment account | 25,078 | 21,877 |
| Loan substitute | 394 | 438 |
| | 93,800 | 80,507 |
| Assets purchased under reverse repurchase agreements | 35,831 | 35,870 |
| Loans | | |
| Residential mortgage | 72,840 | 67,442 |
| Personal | 31,956 | 32,511 |
| Credit card | 4,914 | 4,283 |
| Business and government | 61,751 | 67,152 |
| | 171,461 | 171,388 |
| Allowance for loan losses | (2,203) | (2,278) |
| | 169,258 | 169,110 |
| Other | | |
| Customers' liability under acceptances | 8,051 | 9,923 |
| Derivative-related amounts | 30,258 | 27,240 |
| Premises and equipment | 1,653 | 1,602 |
| Goodwill | 5,004 | 4,919 |
| Other intangibles | 665 | 619 |
| Other assets | 11,113 | 11,935 |
| | 56,744 | 56,238 |
| | \$ 376,956 | \$ 359,260 |
| Liabilities and shareholders' equity | | |
| Deposits | | |
| Personal | \$ 101,892 | \$ 101,381 |
| Business and government | 119,591 | 107,141 |
| Bank | 22,003 | 24,925 |
| | 243,486 | 233,447 |
| Other | | |
| Acceptances | 8,051 | 9,923 |
| Obligations related to securities sold short | 19,110 | 16,443 |
| Obligations related to assets sold under repurchase agreements | 21,109 | 20,864 |
| Derivative-related amounts | 32,137 | 28,646 |
| Other liabilities | 26,197 | 23,780 |
| | 106,604 | 99,656 |
| Subordinated debentures | 6,614 | 6,513 |
| Non-controlling interest in subsidiaries | 1,469 | 1,479 |
| Shareholders' equity | | |
| Capital stock | | |
| Preferred | 1,545 | 2,024 |
| Common (shares issued and outstanding – 665,257,068 and 674,020,927) | 7,057 | 6,973 |
| Retained earnings | 10,181 | 9,168 |
| | 18,783 | 18,165 |
| | \$ 376,956 | \$ 359,260 |

Gordon M. Nixon
President & Chief Executive Officer

Robert B. Peterson
Director

Consolidated statement of income

| For the year ended October 31 (\$ millions) | 2002 | 2001 | 2000 |
|--|-----------------|-----------------|-----------------|
| Interest income | | | |
| Loans | \$ 10,463 | \$ 12,032 | \$ 11,538 |
| Securities | 3,075 | 3,281 | 2,669 |
| Assets purchased under reverse repurchase agreements | 651 | 1,163 | 1,078 |
| Deposits with banks | 483 | 831 | 824 |
| | 14,672 | 17,307 | 16,109 |
| Interest expense | | | |
| Deposits | 5,709 | 8,712 | 9,057 |
| Other liabilities | 1,399 | 1,668 | 1,429 |
| Subordinated debentures | 406 | 410 | 344 |
| | 7,514 | 10,790 | 10,830 |
| Net interest income | 7,158 | 6,517 | 5,279 |
| Provision for credit losses | 1,065 | 1,119 | 691 |
| | 6,093 | 5,398 | 4,588 |
| Other income | | | |
| Capital market fees | 1,866 | 1,523 | 1,538 |
| Trading revenues | 1,766 | 1,820 | 1,540 |
| Investment management and custodial fees | 1,179 | 1,096 | 860 |
| Deposit and payment service charges | 1,041 | 887 | 756 |
| Mutual fund revenues | 723 | 692 | 624 |
| Card service revenues | 496 | 458 | 420 |
| Foreign exchange revenue, other than trading | 279 | 312 | 299 |
| Credit fees | 223 | 237 | 212 |
| Mortgage banking revenues | 222 | 206 | – |
| Insurance revenues | 204 | 201 | 191 |
| Securitization revenues | 174 | 123 | 115 |
| Loss on sale of securities | (116) | (128) | (11) |
| Gain from divestitures | – | 445 | – |
| Other | 505 | 343 | 188 |
| | 8,562 | 8,215 | 6,732 |
| Non-interest expense | | | |
| Human resources | 6,315 | 5,723 | 4,651 |
| Occupancy | 796 | 724 | 570 |
| Equipment | 820 | 771 | 665 |
| Communications | 801 | 686 | 695 |
| Professional fees | 419 | 412 | 267 |
| Amortization of goodwill | – | 248 | 76 |
| Amortization of other intangibles | 72 | 36 | 11 |
| Other | 1,197 | 1,155 | 646 |
| | 10,420 | 9,755 | 7,581 |
| Net income before income taxes | 4,235 | 3,858 | 3,739 |
| Income taxes | 1,365 | 1,340 | 1,445 |
| Net income before non-controlling interest | 2,870 | 2,518 | 2,294 |
| Non-controlling interest in net income of subsidiaries | 108 | 107 | 20 |
| Net income | \$ 2,762 | \$ 2,411 | \$ 2,274 |
| Preferred share dividends | 98 | 135 | 134 |
| Net income available to common shareholders | \$ 2,664 | \$ 2,276 | \$ 2,140 |
| Average number of common shares (in thousands) | 672,571 | 641,516 | 606,389 |
| Earnings per share (in dollars) | \$ 3.96 | \$ 3.55 | \$ 3.53 |
| Average number of diluted common shares (in thousands) | 678,120 | 647,216 | 609,865 |
| Diluted earnings per share (in dollars) | \$ 3.93 | \$ 3.52 | \$ 3.51 |

Consolidated statement of changes in shareholders' equity

| For the year ended October 31 (\$ millions) | 2002 | 2001 | 2000 |
|---|------------------|------------------|------------------|
| Preferred shares | | | |
| Balance at beginning of year | \$ 2,024 | \$ 2,037 | \$ 2,009 |
| Issued | — | 250 | — |
| Redeemed for cancellation | (468) | (300) | — |
| Translation adjustment on shares denominated in foreign currency | (11) | 37 | 28 |
| Balance at end of year | 1,545 | 2,024 | 2,037 |
| Common shares | | | |
| Balance at beginning of year | 6,973 | 3,076 | 3,065 |
| Issued | 236 | 4,009 | 109 |
| Purchased for cancellation | (152) | (112) | (98) |
| Balance at end of year | 7,057 | 6,973 | 3,076 |
| Retained earnings | | | |
| Balance at beginning of year | 9,168 | 8,428 | 7,541 |
| Net income | 2,762 | 2,411 | 2,274 |
| Preferred share dividends | (98) | (135) | (134) |
| Common share dividends | (1,022) | (897) | (689) |
| Cumulative effect of initial adoption of <i>Employee Future Benefits</i> accounting standard, net of related income taxes | — | (221) | — |
| Premium paid on common shares purchased for cancellation | (612) | (397) | (562) |
| Issuance costs, net of related income taxes | (1) | (19) | (4) |
| Change in unrealized foreign currency translation gains and losses | (59) | 473 | (2) |
| Impact of hedging unrealized foreign currency translation gains and losses, net of related income taxes | 43 | (475) | 4 |
| Balance at end of year | 10,181 | 9,168 | 8,428 |
| Shareholders' equity at end of year | \$ 18,783 | \$ 18,165 | \$ 13,541 |

Consolidated statement of cash flows

For the year ended October 31 (\$ millions)

| | 2002 | 2001 | 2000 |
|--|-----------------|-----------------|-----------------|
| Cash flows from operating activities | | | |
| Net income | \$ 2,762 | \$ 2,411 | \$ 2,274 |
| Adjustments to determine net cash provided by (used in) operating activities | | | |
| Provision for credit losses | 1,065 | 1,119 | 691 |
| Depreciation | 407 | 389 | 370 |
| Restructuring | — | 91 | — |
| Amortization of goodwill and other intangibles | 72 | 284 | 87 |
| Deferred income taxes | 98 | (165) | (193) |
| Gain on sale of premises and equipment | (35) | (42) | (4) |
| Gain on divestitures | — | (445) | — |
| Gain on loan securitizations | (54) | (29) | — |
| Loss on sale of investment account securities | 116 | 128 | 11 |
| Changes in operating assets and liabilities | | | |
| Net change in accrued interest receivable and payable | (263) | (142) | 78 |
| Current income taxes | 419 | (460) | (434) |
| Derivative-related assets | (3,018) | (8,076) | (4,004) |
| Derivative-related liabilities | 3,491 | 10,070 | 3,355 |
| Trading account securities | (10,136) | (11,836) | (12,493) |
| Obligations related to securities sold short | 2,667 | 2,869 | (4,466) |
| Other | (614) | (3,373) | 399 |
| Net cash used in operating activities | (3,023) | (7,207) | (14,329) |
| Cash flows from investing activities | | | |
| Change in interest-bearing deposits with banks | (3,046) | (135) | 5,125 |
| Increase in loans, net of loan securitizations | (3,087) | (2,930) | (12,213) |
| Proceeds from loan securitizations | 1,691 | 1,720 | — |
| Proceeds from sale of investment account securities | 16,388 | 12,503 | 10,947 |
| Proceeds from maturity of investment account securities | 15,717 | 14,021 | 16,769 |
| Purchases of investment account securities | (33,093) | (27,494) | (24,453) |
| Decrease in loan substitute securities | 44 | 27 | 70 |
| Net acquisitions of premises and equipment | (419) | (370) | (281) |
| Net proceeds from sale of real estate | — | 57 | — |
| Change in assets purchased under reverse repurchase agreements | 39 | (17,474) | 1,969 |
| Net cash used in acquisition of subsidiaries | (99) | (3,120) | (323) |
| Net proceeds from divestitures | — | 478 | — |
| Net cash used in investing activities | (5,865) | (22,717) | (2,390) |
| Cash flows from financing activities | | | |
| Issue of RBC Trust Capital Securities (RBC TruCS) | — | 750 | 650 |
| Increase in deposits | 8,085 | 19,225 | 14,882 |
| Issue of subordinated debentures | 635 | 1,025 | 1,200 |
| Maturity of subordinated debentures | (101) | (42) | (20) |
| Redemption of subordinated debentures | (400) | (538) | — |
| Issue of preferred shares | — | 250 | — |
| Redemption of preferred shares for cancellation | (468) | (300) | — |
| Issuance costs | (1) | (19) | (4) |
| Issue of common shares | 168 | 657 | 59 |
| Purchase of common shares for cancellation | (764) | (509) | (660) |
| Payment of dividends | (1,104) | (972) | (791) |
| Change in obligations related to assets sold under repurchase agreements | 245 | 11,629 | (391) |
| Change in short-term borrowings of subsidiaries | 3,335 | (387) | 281 |
| Net cash provided by financing activities | 9,630 | 30,769 | 15,206 |
| Net change in cash and due from banks | 742 | 845 | (1,513) |
| Cash and due from banks at beginning of year | 1,792 | 947 | 2,460 |
| Cash and due from banks at end of year | \$ 2,534 | \$ 1,792 | \$ 947 |
| Supplemental disclosure of cash flow information | | | |
| Amount of interest paid in year | \$ 8,229 | \$ 11,149 | \$ 10,698 |
| Amount of income taxes paid in year | \$ 738 | \$ 1,443 | \$ 2,007 |

NOTE 1 Significant accounting policies

Pursuant to the *Bank Act*, these consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles (GAAP), including the accounting requirements of the Superintendent of Financial Institutions Canada. We have also prepared consolidated financial statements in accordance with United States GAAP and these have been provided to shareholders. Note 23 of the consolidated financial statements describes and reconciles the differences between Canadian and United States GAAP.

GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements. Actual results could differ from those estimates.

Certain comparative amounts have been reclassified to conform with the current year's presentation.

The significant accounting policies followed in the preparation of these consolidated financial statements are summarized below:

Basis of consolidation

The consolidated financial statements include the assets and liabilities and results of operations of all subsidiaries after elimination of inter-company transactions and balances. We have accounted for the acquisition of subsidiaries using the purchase method. The equity method is used to account for investments in associated corporations in which the bank has significant influence. These investments are reported in Other assets. Our share of earnings, and gains and losses realized on dispositions of these investments are included in Other income. The proportionate consolidation method is used to account for investments in which we exercise joint control, whereby our pro rata share of assets, liabilities, income and expenses are consolidated.

Translation of foreign currencies

Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at rates prevailing on the balance sheet date; income and expenses are translated at average rates of exchange for the year.

Unrealized foreign currency translation gains and losses (net of hedging activities and related income taxes) on investments in foreign branches, subsidiaries and associated corporations where the functional currency is other than the Canadian dollar are recorded in Retained earnings. On disposal of such investments, the accumulated net translation gain or loss is included in Other income. Other foreign currency translation gains and losses (net of hedging activities) are included in Other income.

Securities

Securities are classified, based on management's intentions, as Trading account or Investment account.

Trading account securities, which are purchased for sale in the near term, are reported at estimated fair value. Obligations to deliver trading account securities sold but not yet purchased are recorded as liabilities and carried at fair value. Realized and unrealized gains and losses on these securities are recorded as Trading revenues in Other income. Dividend and interest income accruing on Trading account securities is recorded in Interest income. Interest expense accruing on interest-bearing securities sold short is recorded in Interest expense.

Investment account securities include securities that may be sold in response to or in anticipation of changes in interest rates and resulting prepayment risk, changes in foreign currency risk, changes in funding sources or terms, or to meet liquidity needs. Investment account equity securities are carried at cost and investment account debt securities at amortized cost. Dividend and interest income is recorded in Interest income. Premiums and discounts on debt securities are amortized to Interest income using the effective yield method over the term to

maturity of the related securities. Gains and losses realized on disposal of securities, which are calculated on an average cost basis, and write-downs to reflect other than temporary impairment in value are included in Loss on sale of securities in Other income.

Loan substitute securities are client financings that have been structured as after-tax investments rather than conventional loans in order to provide the issuers with a borrowing rate advantage. Such securities are accorded the accounting treatment applicable to loans and, if required, are reduced by an allowance for credit losses.

Assets purchased under reverse repurchase agreements and sold under repurchase agreements

We purchase securities under agreements to resell (reverse repurchase agreements) and sell securities under agreements to repurchase (repurchase agreements). Reverse repurchase agreements are treated as collateralized lending transactions and are carried on the Consolidated balance sheet at the amounts at which the securities were initially acquired. Repurchase agreements are treated as collateralized borrowing transactions and are carried on the Consolidated balance sheet at the amounts at which the securities were initially sold, plus accrued interest on interest-bearing securities. Interest earned on reverse repurchase agreements and interest incurred on repurchase agreements are included in Interest income and Interest expense, respectively.

Loans

Loans are stated net of an allowance for loan losses and unearned income, which comprises unearned interest and unamortized loan fees.

Loans are classified as impaired when there is no longer reasonable assurance of the timely collection of the full amount of principal or interest. Whenever a payment is 90 days past due, loans other than credit card balances and Canadian government guaranteed loans are classified as impaired unless they are fully secured or collection efforts are reasonably expected to result in repayment of debt. Credit card balances are written off when a payment is 180 days in arrears. Canadian government guaranteed loans are classified as impaired when the loan is contractually 365 days in arrears. When a loan is identified as impaired, the accrual of interest is discontinued and any previously accrued but unpaid interest on the loan is charged to the Provision for credit losses. Interest received on impaired loans is credited to the Allowance for loan losses on that loan. Impaired loans are returned to performing status when all amounts including interest have been collected, all charges for loan impairment have been reversed and the credit quality has improved such that there is reasonable assurance of timely collection of principal and interest.

When a loan has been identified as impaired, the carrying amount of the loan is reduced to its estimated realizable amount, measured by discounting the expected future cash flows at the effective interest rate inherent in the loan. In subsequent periods, recoveries of amounts previously written off and any increase in the carrying value of the loan is credited to the Provision for credit losses on the consolidated income statement. Where a portion of a loan is written off and the remaining balance is restructured, the new loan is carried on an accrual basis when there is no longer any reasonable doubt regarding the collectibility of principal or interest, and payments are not 90 days past due.

Collateral is obtained if, based on an evaluation of the client's creditworthiness, it is considered necessary for the client's overall borrowing facility.

Assets acquired in respect of problem loans are recorded at the lower of their fair value or the carrying value of the loan at the date of transfer. Any excess of the carrying value of the loan over the fair value of the assets acquired is recognized by a charge to the provision for loan losses.

Fees that relate to such activities as originating, restructuring or renegotiating loans are deferred and recognized as Interest income over the expected term of such loans. Where there is reasonable expectation that a loan will result, commitment and standby fees are also recognized as Interest income over the expected term of the resulting loan. Otherwise, such fees are recorded as Other liabilities and amortized to Other income over the commitment or standby period.

Allowance for credit losses

The allowance for credit losses is maintained at a level that management considers adequate to absorb identified credit related losses in the portfolio as well as losses that have been incurred, but are not yet identifiable. The allowance relates primarily to loans but also to deposits with banks, derivatives, loan substitute securities and other credit instruments such as acceptances, guarantees and letters of credit. The allowance is increased by the Provision for credit losses, which is charged to income, and decreased by the amount of write-offs, net of recoveries.

The allowance is determined based on management's identification and evaluation of problem accounts; estimated probable losses that exist on the remaining portfolio; and on other factors including the composition and quality of the portfolio, and changes in economic conditions.

Specific

Specific allowances are maintained to absorb losses on both specifically identified borrowers and other more homogeneous loans that have become impaired. The losses relating to identified large business and government debtors are estimated based on the present value of expected payments on an account-by-account basis. The losses relating to other portfolio-type products, excluding credit cards, are based on net write-off experience over an economic cycle. For credit cards, no specific allowance is maintained as balances are written off if no payment has been received after 180 days. Personal loans are generally written off at 150 days past due. Write-offs for other loans are generally recorded when there is no realistic prospect of full recovery.

General allocated

The general allocated allowance represents the best estimate of probable losses within the portion of the portfolio that has not yet been specifically identified as impaired. This amount is established quarterly through the application of expected loss factors to outstanding and undrawn facilities. The general allocated allowance for large business and government loans and acceptances is based on the application of expected default and loss factors, determined by statistical loss migration analysis, delineated by loan type and rating. For more homogeneous portfolios, such as residential mortgages, small business loans, personal loans and credit cards, the determination of the general allocated allowance is done on a product portfolio basis. The losses are determined by the application of loss ratios determined through the analysis of loss migration and write-off trends over an economic cycle, adjusted to reflect changes in the product offerings and credit quality of the pool.

General unallocated

The general unallocated allowance is based on management's assessment of probable, unidentified losses in the portfolio that have not been

captured in the determination of the specific or general allocated allowances. This assessment evaluated quarterly includes consideration of general economic and business conditions and regulatory requirements affecting key lending operations, recent loan loss experience, and trends in credit quality and concentrations. This allowance also reflects model and estimation risks and does not represent future losses or serve as a substitute for other allowances.

Acceptances

Acceptances are short-term negotiable instruments issued by our customers to third parties, which we guarantee. The potential liability under acceptances is reported as a liability in the Consolidated balance sheet. The recourse against the customer in the case of a call on these commitments is reported as a corresponding asset of the same amount in Other assets. Fees earned are reported in Other income.

Derivatives

Derivatives are used in sales and trading activities to provide clients with the ability to manage their market risk exposures. We also use derivatives to manage our exposures to interest, currency and other market risks. The most frequently used derivative products are foreign exchange forward contracts, interest rate and currency swaps, foreign currency and interest rate futures, forward rate agreements, foreign currency and interest rate options, and credit derivatives.

When used in sales and trading activities, the realized and unrealized gains and losses on derivatives are recognized in Other income. Market values are determined using pricing models that incorporate current market and contractual prices of the underlying instruments, time value of money, yield curve and volatility factors. A portion of the market value is deferred within Derivative-related amounts in liabilities and amortized to income over the life of the instruments to cover credit risk and ongoing direct servicing costs. Unrealized gains and losses are generally reported on a gross basis as Derivative-related amounts in assets and liabilities, except where we have both the legal right and intent to settle these amounts simultaneously in which case they are presented on a net basis. Margin requirements and premiums paid are also included in Derivative-related amounts in assets, while premiums received are shown in Derivative-related amounts in liabilities.

When we use derivatives to manage our exposures, the income or expense is recognized over the life of the transaction as an adjustment to interest income or expense. Where derivatives have been designated and function effectively as hedges, realized gains and losses are deferred and amortized over the life of hedged assets or liabilities as adjustments to Interest income or Interest expense.

Premises and equipment

Premises and equipment are stated at cost less accumulated depreciation. Depreciation is recorded principally on the straight-line basis over the estimated useful lives of the assets, which are 25 to 50 years for buildings, 3 to 10 years for computer equipment, 7 to 10 years for furniture, fixtures and other equipment, and lease term plus first option period for leasehold improvements. Gains and losses on disposal are recorded in Other income.

NOTE 1 Significant accounting policies (continued)**Business combinations, goodwill and other intangibles**

Effective November 1, 2001, we adopted the Canadian Institute of Chartered Accountants (CICA) standards on *Goodwill and Other Intangible Assets* and *Business Combinations*.

The *Business Combinations* standard requires that all business combinations be accounted for using the purchase method. Identifiable intangible assets are recognized separately from goodwill and included in Other intangibles. Goodwill represents the excess of the price paid for the acquisition of subsidiaries over the fair value of the net assets acquired. Under the *Goodwill and Other Intangible Assets* standard, goodwill and indefinite life intangibles are no longer amortized but are subject to fair value impairment tests on at least an annual basis. Any impairment of goodwill or intangibles will be recognized as Non-interest expense in the period of impairment. Other intangibles with a finite life are amortized over their estimated useful lives and also tested for impairment.

Income taxes

We use the asset and liability method whereby income taxes reflect the expected future tax consequences of temporary differences between the carrying amounts of assets or liabilities for book purposes compared with tax purposes. Accordingly, a deferred income tax asset or liability is determined for each temporary difference based on the tax rates that are expected to be in effect when the underlying items of income and expense are expected to be realized. Income taxes on the consolidated statement of income include the current and deferred portions of the expense. Income taxes applicable to items charged or credited to Retained earnings are netted with such items.

Net deferred income taxes accumulated as a result of temporary differences are included in Other assets. A valuation allowance is established to reduce deferred income tax assets to the amount expected to be realized. In addition, the consolidated statement of income contains items that are non-taxable or non-deductible for income tax purposes and, accordingly, cause the income tax provision to be different than what it would be if based on statutory rates.

Pensions and other postretirement benefits

We offer a number of benefit plans which provide pension and other benefits to qualified employees. These plans include statutory pension plans, supplemental pension plans, defined contribution plans and health, dental and life insurance plans.

We fund our statutory pension plans and health, dental and life insurance plans annually based on actuarially determined amounts needed to satisfy employee benefit entitlements under current pension regulations. These pension plans provide benefits based on years of service, contributions and average earnings at retirement.

Actuarial valuations are performed on a regular basis to determine the present value of the accrued pension benefits, based on projections of employees' compensation levels to the time of retirement. Investments held by the pension funds primarily comprise of equity securities, bonds and debentures. Pension fund assets are valued at fair value each year.

Pension benefit expense consists of the cost of employee pension benefits for the current year's service, interest cost on the liability, expected investment return on the market-related value of plan assets and the amortization of both unrecognized prior service costs and unrecognized net actuarial gains or losses. Amortization is charged over the expected average remaining service life of employee groups covered by the plan.

The cumulative excess of pension fund contributions over the amounts recorded as expenses is reported as a prepaid pension benefit cost in Other assets. The cumulative excess of pension expense over pension fund contributions is reported as accrued pension benefit expense in Other liabilities. In addition, other postretirement benefits are also reported in Other liabilities.

Defined contribution plan costs are recognized in income for services rendered by employees during the period.

Assets under administration and assets under management

We administer and manage assets owned by clients that are not reflected on the Consolidated balance sheet. Asset management fees are earned for providing investment management services and mutual fund products. Asset administration fees are earned for providing trust, estate administration, custodial services and administration of assets securitized. Fees are recognized and reported in Other income as the services are provided.

Loan securitization

We periodically securitize loans by selling loans to independent special purpose entities or trusts that issue securities to investors. These transactions are accounted for as sales when we are deemed to have surrendered control over such assets and have received in exchange consideration other than beneficial interests in these transferred assets. We often retain interests in the securitized loans, such as interest-only strips or servicing rights, and in some cases cash reserve accounts. Gains on these transactions are recognized in Other income and are dependent in part on the previous carrying amount of the loans involved in the transfer, which is allocated between the loans sold and the retained interests, based on their relative fair value at the date of transfer. To obtain fair values, quoted market prices are used, if available. When quotes are not available for retained interests, we generally determine fair value based on the present value of expected future cash flows using management's best estimates of key assumptions such as payment rates, excess spread, credit losses and discount rates commensurate with the risks involved.

Generally, the loans are transferred on a fully serviced basis. As a result, we recognize a servicing liability on the date of transfer and amortize this liability to income over the term of the transferred loans.

Retained interests in securitizations that can be contractually prepaid or otherwise settled in such a way that we would not recover substantially all of our recorded investment, are classified as Investment account securities.

Insurance operations

Earned premiums, fees, and changes in claims and policy benefit liabilities are included in Other income. Investments are included in Investment account securities and claims and policy benefit liabilities are included in Other liabilities. Investment income is included in Interest income and administrative expenses are included in Non-interest expense.

Premiums from long-duration contracts, primarily life insurance, are recognized as income when due. Premiums from short-duration contracts, primarily property and casualty, and fees for administrative services and investment-type contracts are recognized over the related contract period.

Claims and policy benefit liabilities represent estimates for future insurance policy benefits. Liabilities for life insurance contracts are determined using the Canadian Asset Liability Method (CALM), which incorporates assumptions for mortality, morbidity, policy lapses and surrenders, investment yields, policy dividends, operating and policy maintenance expenses and provision for adverse deviations. These assumptions are updated to reflect the results of the latest empirical tests. Liabilities for property and casualty insurance include unearned premiums, representing the unexpired portion of premiums, and estimated provisions for reported and unreported claims incurred.

Realized gains and losses on disposal of investments that support life insurance liabilities are deferred and amortized to Other income over a maximum period of 20 years. The differences between the market value and adjusted carrying cost of equity securities and real estate investments are reduced annually by 15% and 10%, respectively.

Deferred acquisition costs for life insurance are implicitly recognized in claims and policy benefit liabilities by CALM. For property and casualty insurance these costs are classified as Other assets and amortized over the policy term.

Significant future accounting changes

Hedging relationships

In November 2001, the CICA issued Accounting Guideline 13, *Hedging Relationships* (AcG-13), whose effective date has been postponed by the CICA to fiscal years beginning on or after July 1, 2003. We are early adopting this guideline effective November 1, 2002.

AcG-13 establishes specific criteria for non-trading derivatives to qualify for hedge accounting. Where we intend to apply hedge accounting, a hedge relationship will be designated at inception detailing the particular risk management objective and the strategy for undertaking the hedge transaction. The documentation will identify the specific asset or liability being hedged, the risk that is being hedged, the type of derivative used and how effectiveness will be measured. The derivative must be highly effective in offsetting either changes in the fair value or cash flows attributable to the risk being hedged, both at inception and over the life of the hedge. Where a non-trading derivative has been designated and functions effectively as a hedge, the existing accounting treatment will continue as described earlier in this note. This hedge accounting will

be discontinued prospectively when the derivative ceases to qualify as an effective hedge, and the fair value of the derivative will be recognized on the balance sheet at that time. The amounts required to record the derivative at this fair value will be deferred and recognized in income as the hedged item affects net income. Subsequent changes in fair value will be recognized immediately in Other income until the derivative qualifies for hedge accounting again. The fair value at the time the derivative qualifies again will be recognized in income as the hedged item affects net income.

Non-trading derivatives that do not qualify for hedge accounting under AcG-13 are carried at fair value on the balance sheet effective November 1, 2002. This will increase assets by \$428 million and liabilities by \$395 million. The resulting transition gain of \$33 million will be deferred, further increasing liabilities, and recognized in income as the original hedged item affects net income.

Consolidation of special purpose entities

The CICA issued a draft Accounting Guideline, *Consolidation of Special-Purpose Entities* on August 1, 2002. The proposed guideline provides guidance on determining who is a primary beneficiary of the special purpose entities and will therefore be required to consolidate the special purpose entities. The effect of this proposed guideline cannot be determined at this time.

NOTE 2 Significant acquisitions and dispositions

2002

Acquisitions

During 2002, we completed the acquisitions of the private banking business of Barclays PLC in the Americas (Barclays) and Eagle Bancshares, Inc. (Eagle Bancshares). Goodwill has been estimated using the best available information as at the date of these financial statements

and may be adjusted for up to one year after the closing date of the acquisition in order to incorporate refinements to the initial fair value estimates of assets and liabilities acquired. The details of these acquisitions are as follows:

| | Barclays | Eagle Bancshares |
|---|---|--|
| Acquisition date | June 28, 2002 | July 22, 2002 |
| Business segment | RBC Investments | RBC Banking |
| Percentage of shares acquired | — | 100% |
| Purchase consideration | Assets were purchased with an initial cash payment of approximately US\$111 million. Additional consideration that is contingent upon the amount of business retained is expected to be paid next year and will be recorded as an intangible asset. | Each Eagle Bancshares common share was purchased for US\$26 cash |
| Fair value of tangible assets acquired | \$ 741 | \$ 1,844 |
| Fair value of liabilities assumed | (640) | (1,764) |
| Fair value of identifiable net tangible assets acquired | 101 | 80 |
| Core deposit intangibles (1) | — | 22 |
| Customer lists and relationships (1) | 68 | — |
| Goodwill | — | 133 |
| Total purchase consideration | \$ 169 | \$ 235 |

(1) Core deposit intangibles and customer lists and relationships are amortized on a straight-line basis over an estimated average useful life of 10 and 15 years, respectively.

NOTE 2 Significant acquisitions and dispositions (continued)**Pending acquisitions***Acquisition of certain U.S. operations of Generali Group*

On April 30, 2002, RBC Insurance announced an agreement to acquire certain assets of Generali Group, the Trieste, Italy-based insurer. These assets consist of the operations of Business Men's Assurance Company of America (BMA) and include an inforce block of approximately 150,000 traditional life insurance policies and annuities as well as the infrastructure for manufacturing variable insurance products. In a related transaction, RBC Dain Rauscher plans to acquire BMA's mutual fund company, Jones & Babson Inc.

The purchase price for these businesses is estimated at approximately US\$220 million. The acquisitions are subject to regulatory approvals, approval by shareholders of advisory clients of Jones & Babson Inc., and other customary closing conditions.

Acquisition of Admiralty Bancorp, Inc.

On August 29, 2002, RBC Centura Banks, Inc. (Centura), a wholly owned subsidiary of Royal Bank of Canada, and Admiralty Bancorp, Inc. (Admiralty) announced that they have signed a definitive merger agreement by which Centura will acquire Admiralty. The cash consideration expected to be paid with respect to the acquisition is approximately US\$150 million. The excess of approximately US\$100 million of the purchase price over the estimated fair value of the net tangible assets acquired will first be allocated to identifiable intangible assets, with the residual allocated to Goodwill. The acquisition is subject to regulatory approvals, approval by shareholders of Admiralty, and other customary closing conditions.

2001**Acquisitions**

During 2001, we completed the acquisitions of Liberty Life Insurance Company and Liberty Insurance Services Corporation (Liberty), Dain Rauscher Corporation (Dain Rauscher), Centura Banks, Inc. (Centura)

and Tucker Anthony Suto Corporation (Tucker Anthony Suto). We accounted for all of these acquisitions using the purchase method. The details of these acquisitions are as follows:

| | Liberty | Dain Rauscher | Centura | Tucker Anthony Suto |
|---|--|---|---|---|
| Acquisition date | November 1, 2000 | January 10, 2001 | June 5, 2001 | October 31, 2001 |
| Business segment | RBC Insurance | RBC Investments & RBC Capital Markets | RBC Banking | RBC Investments & RBC Capital Markets |
| Percentage of shares acquired | 100% | 100% | 100% | 100% |
| Purchase consideration | Assets were purchased with a dividend of US\$70 million paid from Liberty Life Insurance Company plus US\$580 million cash | Each Dain Rauscher common share was purchased for US\$95 cash | Approximately 67 million Royal Bank common shares were issued, valued at \$49.20 each | Each Tucker Anthony Suto common share was purchased for US\$24 cash |
| Fair value of tangible assets acquired | \$ 2,084 | \$ 3,719 | \$ 18,270 | \$ 831 |
| Fair value of liabilities assumed | (1,383) | (3,425) | (17,214) | (580) |
| Fair value of identifiable net tangible assets acquired | 701 | 294 | 1,056 | 251 |
| Core deposit intangibles (1) | — | — | 395 | — |
| Mortgage servicing rights (1) | — | — | 12 | — |
| Goodwill | 189 | 1,544 | 1,868 | 692 |
| Total purchase consideration | \$ 890 | \$ 1,838 | \$ 3,331 | \$ 943 |

(1) Core deposit intangibles and mortgage servicing rights are amortized on a straight-line basis over an estimated average useful life of 10 and 5 years, respectively.

Dispositions

During 2001, we sold our institutional asset management business operated by RT Capital Management Inc. and realized a pre-tax gain of \$313 million (after-tax \$251 million) recorded in Other income.

In addition, we divested certain other businesses and realized a pre-tax gain of \$132 million (after-tax \$111 million) recorded in Other income.

NOTE 3 Results by business and geographic segment

| 2002 | RBC Banking | RBC Insurance | RBC Investments | RBC Capital Markets | RBC Global Services | Other | Total | Canada | United States | Other Inter- national |
|--|----------------|------------------|--------------------|------------------------|------------------------|----------|------------|------------|------------------|-----------------------------|
| Net interest income on taxable equivalent basis | \$ 5,576 | \$ 223 | \$ 371 | \$ 553 | \$ 137 | \$ 338 | \$ 7,198 | \$ 5,556 | \$ 1,262 | \$ 380 |
| Taxable equivalent adjustment | 19 | — | — | 21 | — | — | 40 | 24 | 16 | — |
| Net interest income | 5,557 | 223 | 371 | 532 | 137 | 338 | 7,158 | 5,532 | 1,246 | 380 |
| Provision for credit losses | 626 | — | (1) | 465 | 10 | (35) | 1,065 | 529 | 440 | 96 |
| Other income | 4,931 | 223 | 372 | 67 | 127 | 373 | 6,093 | 5,003 | 806 | 284 |
| Income taxes | 2,073 | 285 | 3,274 | 2,112 | 820 | (2) | 8,562 | 4,411 | 3,040 | 1,111 |
| Non-interest expense | 4,528 | 437 | 3,146 | 1,627 | 668 | 14 | 10,420 | 5,920 | 3,676 | 824 |
| Net income before income taxes | 2,476 | 71 | 500 | 552 | 279 | 357 | 4,235 | 3,494 | 170 | 571 |
| Income taxes | 937 | (46) | 157 | 135 | 108 | 74 | 1,365 | 1,308 | 14 | 43 |
| Non-controlling interest | 8 | — | — | — | — | 100 | 108 | 100 | 2 | 6 |
| Net income (loss) | \$ 1,531 | \$ 117 | \$ 343 | \$ 417 | \$ 171 | \$ 183 | \$ 2,762 | \$ 2,086 | \$ 154 | \$ 522 |
| Total average assets | \$ 156,500 | \$ 5,600 | \$ 15,100 | \$ 178,200 | \$ 2,500 | \$ 9,400 | \$ 367,300 | \$ 225,700 | \$ 72,600 | \$ 69,000 |

| 2001 | RBC Banking | RBC Insurance | RBC Investments | RBC Capital Markets | RBC Global Services | Other | Total | Canada | United States | Other Inter- national |
|--|----------------|------------------|--------------------|------------------------|------------------------|----------|------------|------------|------------------|-----------------------------|
| Net interest income on taxable equivalent basis | \$ 5,349 | \$ 206 | \$ 385 | \$ 430 | \$ 147 | \$ 32 | \$ 6,549 | \$ 5,614 | \$ 485 | \$ 450 |
| Taxable equivalent adjustment | 6 | — | — | 21 | — | 5 | 32 | 30 | 2 | — |
| Net interest income | 5,343 | 206 | 385 | 409 | 147 | 27 | 6,517 | 5,584 | 483 | 450 |
| Provision for credit losses | 732 | — | 2 | 407 | (2) | (20) | 1,119 | 757 | 379 | (17) |
| Other income | 4,611 | 206 | 383 | 2 | 149 | 47 | 5,398 | 4,827 | 104 | 467 |
| Income taxes | 1,869 | 274 | 2,861 | 2,346 | 851 | 14 | 8,215 | 4,972 | 2,355 | 888 |
| Non-interest expense | 4,389 | 375 | 2,607 | 1,804 | 599 | 81 | 9,755 | 6,326 | 2,715 | 714 |
| Net income before income taxes | 2,091 | 105 | 737 | 544 | 401 | (20) | 3,858 | 3,473 | (256) | 641 |
| Income taxes | 900 | (28) | 224 | 208 | 138 | (102) | 1,340 | 1,410 | (85) | 15 |
| Non-controlling interest | 10 | — | — | — | — | 97 | 107 | 97 | 2 | 8 |
| Net income (loss) | \$ 1,181 | \$ 133 | \$ 513 | \$ 336 | \$ 263 | \$ (15) | \$ 2,411 | \$ 1,966 | \$ (173) | \$ 618 |
| Total average assets | \$ 143,100 | \$ 5,300 | \$ 11,200 | \$ 156,400 | \$ 2,400 | \$ 8,700 | \$ 327,100 | \$ 210,500 | \$ 50,200 | \$ 66,400 |

| 2000 | RBC Banking | RBC Insurance | RBC Investments | RBC Capital Markets | RBC Global Services | Other | Total | Canada | United States | Other Inter- national |
|--|----------------|------------------|--------------------|------------------------|------------------------|----------|------------|------------|------------------|-----------------------------|
| Net interest income on taxable equivalent basis | \$ 4,705 | \$ 84 | \$ 359 | \$ 43 | \$ 160 | \$ (44) | \$ 5,307 | \$ 5,029 | \$ (17) | \$ 295 |
| Taxable equivalent adjustment | 6 | — | — | 22 | — | — | 28 | 28 | — | — |
| Net interest income | 4,699 | 84 | 359 | 21 | 160 | (44) | 5,279 | 5,001 | (17) | 295 |
| Provision for credit losses | 649 | — | (1) | 91 | (21) | (27) | 691 | 646 | 99 | (54) |
| Other income | 4,050 | 84 | 360 | (70) | 181 | (17) | 4,588 | 4,355 | (116) | 349 |
| Income taxes | 1,570 | 202 | 1,958 | 2,287 | 691 | 24 | 6,732 | 4,997 | 856 | 879 |
| Non-interest expense | 3,752 | 173 | 1,658 | 1,445 | 547 | 6 | 7,581 | 6,198 | 640 | 743 |
| Net income before income taxes | 1,868 | 113 | 660 | 772 | 325 | 1 | 3,739 | 3,154 | 100 | 485 |
| Income taxes | 785 | (19) | 244 | 264 | 140 | 31 | 1,445 | 1,467 | 29 | (51) |
| Non-controlling interest | 5 | — | — | — | — | 15 | 20 | 15 | — | 5 |
| Net income (loss) | \$ 1,078 | \$ 132 | \$ 416 | \$ 508 | \$ 185 | \$ (45) | \$ 2,274 | \$ 1,672 | \$ 71 | \$ 531 |
| Total average assets | \$ 129,700 | \$ 2,100 | \$ 8,000 | \$ 131,900 | \$ 1,600 | \$ 8,600 | \$ 281,900 | \$ 196,600 | \$ 34,700 | \$ 50,600 |

For management reporting purposes, our operations are grouped into the business segments of RBC Banking, RBC Insurance, RBC Investments, RBC Capital Markets and RBC Global Services. The Other segment mainly comprises Corporate Treasury, Corporate Resources, Systems & Technology and Real Estate Operations.

The business segments operate on an arm's-length basis with respect to the purchase and sale of intra-group services. Transfer pricing

of funds sold or purchased, commissions, or charges and credits for services rendered are generally at market rates.

For geographic reporting purposes, our operations are grouped into Canada, United States and Other International. Canadian-based activities of international money market units are included in United States and Other International.

NOTE 4 Goodwill and Other intangibles

Effective November 1, 2001, we adopted the Canadian Institute of Chartered Accountants (CICA) standard on *Goodwill and other intangible assets*. Under this standard, goodwill impairment is assessed at the reporting unit level on at least an annual basis. Reporting units comprise business operations with similar economic characteristics and strategies and may represent either a business segment or a business unit within a business segment.

We have completed both the transitional and annual test for goodwill impairment in all reporting units and have determined that goodwill is not impaired.

The projected amortization of Other intangibles for each of the years ending October 31, 2003 to October 31, 2007 is approximately \$76 million.

Goodwill

| | RBC Banking | RBC Insurance | RBC Investments | RBC Capital Markets | RBC Global Services | Total |
|--|-------------|---------------|-----------------|---------------------|---------------------|----------|
| Balance at October 31, 2000 | \$ 200 | \$ 4 | \$ 241 | \$ 80 | \$ 123 | \$ 648 |
| Goodwill acquired during the year | 1,868 | 189 | 1,618 | 618 | 10 | 4,303 |
| Amortization of goodwill during the year | (61) | (15) | (78) | (42) | (14) | (210) |
| Goodwill impairment | — | — | (38) | — | — | (38) |
| Other adjustments (1) | 98 | 26 | 39 | 55 | (2) | 216 |
| Balance at October 31, 2001 | 2,105 | 204 | 1,782 | 711 | 117 | 4,919 |
| Goodwill acquired during the year | 143 | — | — | — | 2 | 145 |
| Other adjustments (1) | (19) | (8) | (21) | (14) | 2 | (60) |
| Balance at October 31, 2002 | \$ 2,229 | \$ 196 | \$ 1,761 | \$ 697 | \$ 121 | \$ 5,004 |

(1) Other adjustments include foreign exchange translations on non-Canadian dollar denominated goodwill and certain other adjustments.

Other intangibles

| | 2002 | | | 2001 | | |
|----------------------------------|-----------------------|--------------------------|---------------------|-----------------------|--------------------------|---------------------|
| | Gross carrying amount | Accumulated amortization | Net carrying amount | Gross carrying amount | Accumulated amortization | Net carrying amount |
| Core deposit intangibles | \$ 423 | \$ (50) | \$ 373 | \$ 412 | \$ (17) | \$ 395 |
| Customer lists and relationships | 318 | (52) | 266 | 233 | (30) | 203 |
| Mortgage servicing rights | 41 | (18) | 23 | 17 | (1) | 16 |
| Other intangibles | 5 | (2) | 3 | 7 | (2) | 5 |
| Total | \$ 787 | \$ (122) | \$ 665 | \$ 669 | \$ (50) | \$ 619 |

The following table discloses a reconciliation of reported net income, earnings per share and diluted earnings per share to the amounts adjusted for the exclusion of Amortization of goodwill, net of related income taxes.

| | 2002 | 2001 | 2000 |
|---|----------|----------|----------|
| Net income: | | | |
| Reported net income | \$ 2,762 | \$ 2,411 | \$ 2,274 |
| Amortization of goodwill, net of related income taxes | — | 246 | 73 |
| Adjusted net income | \$ 2,762 | \$ 2,657 | \$ 2,347 |
| Earnings per share: | | | |
| Reported earnings per share | \$ 3.96 | \$ 3.55 | \$ 3.53 |
| Amortization of goodwill, net of related income taxes | — | .38 | .12 |
| Adjusted earnings per share | \$ 3.96 | \$ 3.93 | \$ 3.65 |
| Diluted earnings per share: | | | |
| Reported diluted earnings per share | \$ 3.93 | \$ 3.52 | \$ 3.51 |
| Amortization of goodwill, net of related income taxes | — | .38 | .12 |
| Adjusted diluted earnings per share | \$ 3.93 | \$ 3.90 | \$ 3.63 |

NOTE 5 Securities

| | Term to maturity (1) | | | | | 2002 Total | 2001 Total |
|---|----------------------|-----------------|-----------------------------|------------------|---------------------------------|-----------------|-----------------|
| | Under 1 year | 1 to 5 years | Over 5 years to 10 years | Over 10 years | With no specific maturity | | |
| Trading account (2) | | | | | | | |
| Canadian government debt | \$ 5,171 | \$ 4,690 | \$ 1,620 | \$ 1,469 | \$ – | \$12,950 | \$13,032 |
| U.S. Treasury and other U.S. agencies | 278 | 809 | 560 | 32 | – | 1,679 | 953 |
| Other OECD government debt | 618 | 1,223 | 1,254 | 738 | – | 3,833 | 2,413 |
| Mortgage-backed securities | 71 | 99 | 86 | 327 | – | 583 | 689 |
| Asset-backed securities | 66 | 247 | 2,704 | 3,523 | – | 6,540 | 4,428 |
| Other debt | 9,355 | 4,237 | 1,942 | 2,887 | 579 | 19,000 | 21,252 |
| Equities | – | – | – | – | 23,743 | 23,743 | 15,425 |
| | 15,559 | 11,305 | 8,166 | 8,976 | 24,322 | 68,328 | 58,192 |
| Investment account (2) | | | | | | | |
| Canadian government debt | | | | | | | |
| Amortized cost | 1,943 | 2,826 | 503 | 247 | – | 5,519 | 4,623 |
| Estimated fair value | 1,945 | 2,883 | 510 | 275 | – | 5,613 | 4,708 |
| Yield (3) | 4.0% | 4.5% | 5.3% | 6.6% | – | 4.5% | 4.9% |
| U.S. Treasury and other U.S. agencies | | | | | | | |
| Amortized cost | 544 | 1,204 | 319 | 1 | – | 2,068 | 2,030 |
| Estimated fair value | 552 | 1,280 | 355 | 1 | – | 2,188 | 2,118 |
| Yield (3) | 4.0% | 5.0% | 3.9% | 6.0% | – | 4.6% | 4.8% |
| Other OECD government debt | | | | | | | |
| Amortized cost | 2,308 | 291 | 6 | – | – | 2,605 | 1,561 |
| Estimated fair value | 2,324 | 303 | 6 | – | – | 2,633 | 1,573 |
| Yield (3) | .3% | 3.7% | 4.7% | – | – | .7% | 1.2% |
| Mortgage-backed securities | | | | | | | |
| Amortized cost | 1,126 | 2,730 | 294 | 435 | – | 4,585 | 4,531 |
| Estimated fair value | 1,136 | 2,782 | 312 | 457 | – | 4,687 | 4,676 |
| Yield (3) | 5.0% | 5.0% | 7.2% | 6.5% | – | 5.3% | 5.6% |
| Asset-backed securities | | | | | | | |
| Amortized cost | – | 98 | 154 | 75 | – | 327 | 414 |
| Estimated fair value | – | 98 | 163 | 83 | – | 344 | 434 |
| Yield (3) | – | 8.3% | 6.8% | 6.6% | – | 7.2% | 8.2% |
| Other debt | | | | | | | |
| Amortized cost | 2,263 | 1,490 | 592 | 4,198 | 159 | 8,702 | 7,331 |
| Estimated fair value | 2,258 | 1,527 | 613 | 4,267 | 159 | 8,824 | 7,375 |
| Yield (3) | 2.3% | 4.1% | 6.3% | 5.5% | 5.1% | 4.5% | 5.5% |
| Equities | | | | | | | |
| Cost | – | – | – | – | 1,272 | 1,272 | 1,387 |
| Estimated fair value | – | – | – | – | 1,240 | 1,240 | 1,423 |
| Amortized cost | 8,184 | 8,639 | 1,868 | 4,956 | 1,431 | 25,078 | 21,877 |
| Estimated fair value | 8,215 | 8,873 | 1,959 | 5,083 | 1,399 | 25,529 | 22,307 |
| Loan substitute (4) | 50 | 344 | – | – | – | 394 | 438 |
| Total carrying value of securities (2) | \$23,793 | \$20,288 | \$10,034 | \$13,932 | \$25,753 | \$93,800 | \$80,507 |
| Total estimated fair value of securities | \$23,824 | \$20,522 | \$10,125 | \$14,059 | \$25,721 | \$94,251 | \$80,937 |

(1) Actual maturities may differ from contractual maturities shown above, since borrowers may have the right to prepay obligations with or without prepayment penalties.

(2) Trading account securities are carried at estimated fair value. Investment account securities are carried at amortized cost for debt securities and cost for equity securities.

(3) The weighted average yield is based on the carrying value at the end of the year for the respective securities.

(4) The carrying value of loan substitute securities approximates estimated fair value.

Unrealized gains and losses on Investment account securities

| | 2002 | | | | 2001 | | | |
|---------------------------------------|-------------------|------------------------------|-------------------------------|----------------------------|-------------------|------------------------------|-------------------------------|----------------------------|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | Estimated fair value | Amortized cost | Gross unrealized gains | Gross unrealized losses | Estimated fair value |
| Canadian government debt | \$ 5,519 | \$ 97 | \$ (3) | \$ 5,613 | \$ 4,623 | \$ 85 | \$ – | \$ 4,708 |
| U.S. Treasury and other U.S. agencies | 2,068 | 120 | – | 2,188 | 2,030 | 88 | – | 2,118 |
| Other OECD government debt | 2,605 | 28 | – | 2,633 | 1,561 | 15 | (3) | 1,573 |
| Mortgage-backed securities | 4,585 | 102 | – | 4,687 | 4,531 | 145 | – | 4,676 |
| Asset-backed securities | 327 | 28 | (11) | 344 | 414 | 25 | (5) | 434 |
| Other debt | 8,702 | 201 | (79) | 8,824 | 7,331 | 169 | (125) | 7,375 |
| Equities | 1,272 | 28 | (60) | 1,240 | 1,387 | 104 | (68) | 1,423 |
| | \$25,078 | \$ 604 | \$ (153) | \$25,529 | \$21,877 | \$ 631 | \$ (201) | \$22,307 |

Realized gains and losses on sale of Investment account securities

| | 2002 | 2001 | 2000 |
|----------------------------|----------|----------|---------|
| Realized gains | \$ 78 | \$ 106 | \$ 106 |
| Realized losses | (194) | (234) | (117) |
| Loss on sale of securities | \$ (116) | \$ (128) | \$ (11) |

NOTE 6 Loans

| | 2002 | 2001 |
|---|-------------------|-------------------|
| Canada (1) | | |
| Residential mortgage | \$ 67,700 | \$ 64,066 |
| Personal | 25,918 | 27,202 |
| Credit card | 4,740 | 4,110 |
| Business and government | 29,778 | 32,682 |
| | 128,136 | 128,060 |
| United States (1) | | |
| Residential mortgage | 4,351 | 2,664 |
| Personal | 5,269 | 4,621 |
| Credit card | 125 | 128 |
| Business and government | 21,412 | 22,414 |
| | 31,157 | 29,827 |
| Other International (1) | | |
| Residential mortgage | 789 | 712 |
| Personal | 769 | 688 |
| Credit card | 49 | 45 |
| Business and government | 10,561 | 12,056 |
| | 12,168 | 13,501 |
| Total loans (2) | 171,461 | 171,388 |
| Allowance for loan losses | (2,203) | (2,278) |
| Total loans net of allowance for loan losses | \$ 169,258 | \$ 169,110 |

(1) Loans in Canada, United States and Other International include all loans booked in those locations, regardless of currency or residence of borrower.
(2) Loans are net of unearned income of \$131 million (2001 – \$130 million).

Loan maturities and rate sensitivity 2002

| | Maturity term | | | | Rate sensitivity | | | |
|---|-------------------|------------------|-----------------|-------------------|------------------|-------------------|--------------------|-------------------|
| | Under 1 year | 1 to 5 years | Over 5 years | Total | Floating | Fixed term | Non-rate-sensitive | Total |
| Residential mortgage | \$ 27,489 | \$ 44,057 | \$ 1,294 | \$ 72,840 | \$ 8,128 | \$ 64,581 | \$ 131 | \$ 72,840 |
| Personal | 30,363 | 1,486 | 107 | 31,956 | 21,934 | 9,716 | 306 | 31,956 |
| Credit card | 4,914 | — | — | 4,914 | — | 3,326 | 1,588 | 4,914 |
| Business and government | 44,986 | 13,242 | 3,523 | 61,751 | 14,054 | 45,846 | 1,851 | 61,751 |
| Total loans | \$ 107,752 | \$ 58,785 | \$ 4,924 | 171,461 | \$ 44,116 | \$ 123,469 | \$ 3,876 | 171,461 |
| Allowance for loan losses | | | | (2,203) | | | | (2,203) |
| Total loans net of allowance for loan losses | | | | \$ 169,258 | | | | \$ 169,258 |

Impaired loans

| | 2002 | | | 2001 |
|-----------------------------|-----------------|--------------------|-----------------|-----------------|
| | Gross | Specific allowance | Net | Net |
| Residential mortgage | \$ 131 | \$ (18) | \$ 113 | \$ 153 |
| Personal | 306 | (177) | 129 | 137 |
| Business and government (1) | 1,851 | (699) | 1,152 | 1,193 |
| | \$ 2,288 | \$ (894) | \$ 1,394 | \$ 1,483 |

(1) Includes specific allowances of \$2 million (2001 – \$5 million) related to loan substitute securities.

Allowance for loan losses

| | 2002 | | | | | | | 2001 |
|---|------------------------------|-------------------|---------------|-----------------------------|--------------------------------------|--------------|------------------------|------------------------|
| | Balance at beginning of year | Write-offs | Recoveries | Provision for credit losses | Eagle Bancshares at acquisition date | Other | Balance at end of year | Balance at end of year |
| Residential mortgage | \$ 49 | \$ (12) | \$ — | \$ 1 | \$ 4 | \$ (1) | \$ 41 | \$ 49 |
| Personal | 480 | (398) | 70 | 283 | 1 | 29 | 465 | 480 |
| Credit card | 152 | (178) | 38 | 140 | — | — | 152 | 152 |
| Business and government (1) | 1,486 | (869) | 90 | 619 | 10 | 69 | 1,405 | 1,486 |
| General unallocated allowance | 225 | — | — | 22 | 3 | 1 | 251 | 225 |
| Total allowance for credit losses | \$ 2,392 | \$ (1,457) | \$ 198 | \$ 1,065 | \$ 18 | \$ 98 | \$ 2,314 | \$ 2,392 |
| Specific allowances | \$ 951 | \$ (1,424) | \$ 198 | \$ 1,065 | \$ 10 | \$ 94 | \$ 894 | \$ 951 |
| Country risk allowances | 31 | (33) | — | — | — | 2 | — | 31 |
| General allowance | | | | | | | | |
| General allocated | 1,185 | — | — | (22) | 5 | 1 | 1,169 | 1,185 |
| General unallocated | 225 | — | — | 22 | 3 | 1 | 251 | 225 |
| Total general allowance for credit losses | 1,410 | — | — | — | 8 | 2 | 1,420 | 1,410 |
| Total allowance for credit losses | \$ 2,392 | \$ (1,457) | \$ 198 | \$ 1,065 | \$ 18 | \$ 98 | \$ 2,314 | \$ 2,392 |
| Allowance for off-balance sheet and other items (2) | (109) | — | — | — | — | — | (109) | (109) |
| Allowance for loan substitute securities | (5) | 9 | — | — | — | (6) | (2) | (5) |
| Total allowance for loan losses | 2,278 | (1,448) | 198 | 1,065 | 18 | 92 | 2,203 | \$ 2,278 |

(1) Includes \$2 million (2001 – \$5 million) related to loan substitute securities and \$109 million (2001 – \$109 million) related to off-balance sheet and other items.

(2) The allowance for off-balance sheet and other items was reported separately under Other liabilities.

NOTE 7 Securitizations

During the year, we securitized \$3,734 million (2001 – \$800 million) of government guaranteed residential mortgage loans through the creation of mortgage-backed securities, and sold \$1,708 million (2001 – \$723 million) of those securities. We received net cash proceeds of \$1,691 million (2001 – \$720 million) and retained the rights to future excess interest of \$71 million (2001 – \$25 million) on the residential mortgages. A pre-tax gain on sale, net of transaction costs, of \$54 million (2001 – \$22 million) was recognized in Securitization revenues. Mortgage-backed securities, created and unsold, remain on the Consolidated balance sheet and are classified as Investment account.

We did not sell any undivided interests in credit card loans during the year (2001 – \$1,000 million).

The key assumptions used to value the retained interests in residential mortgage loans at the date of securitization for transactions completed during the year were an annualized payment rate of 12.00%, excess spread of 1.20%, and discount rate of 4.75%.

Static pool credit losses include actual incurred and projected credit losses divided by the original balance of the loans securitized. The expected static pool credit loss ratio for securitized credit card loans at October 31, 2002 was .41%.

The following table summarizes the loan principal, impaired and net write-offs for total loans reported on our balance sheet and securitized loans that we manage as at October 31, 2002 and 2001:

Loans reported and securitized

| | 2002 | | | 2001 | | |
|--|----------------|--------------|----------------|----------------|--------------|----------------|
| | Loan principal | Impaired (1) | Net write-offs | Loan principal | Impaired (1) | Net write-offs |
| Residential mortgage | \$ 78,321 | \$ 228 | \$ 12 | \$ 71,882 | \$ 283 | \$ 24 |
| Personal | 31,956 | 371 | 328 | 32,511 | 387 | 334 |
| Credit card | 6,589 | 41 | 172 | 6,383 | 49 | 152 |
| Business and government | 61,751 | 1,865 | 779 | 67,152 | 1,991 | 455 |
| Total loans managed (2) | 178,617 | 2,505 | 1,291 | 177,928 | 2,710 | 965 |
| Less: Loans securitized (3) | 7,156 | – | 32 | 6,540 | – | 25 |
| Total loans reported on the Consolidated balance sheet | \$ 171,461 | \$ 2,505 | \$ 1,259 | \$ 171,388 | \$ 2,710 | \$ 940 |

(1) Includes past due loans greater than 90 days not classified as impaired.

(2) Represents net loans outstanding and loans that have been securitized, which we continue to service, and excludes any assets we have temporarily acquired with the intent at acquisition to sell them to special purpose entities.

(3) Loan principal includes credit card loans of \$1,675 million (2001 – \$2,100 million), mortgage-backed securities created and sold of \$2,416 million (2001 – \$1,361 million) and mortgage-backed securities created and unsold of \$3,065 million (2001 – \$3,079 million).

At October 31, 2002, key economic assumptions and the sensitivity of the current fair value of these retained interests to immediate 10% and 20% adverse changes in key assumptions are shown in the first table below.

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in fair value based on a variation in assumptions generally cannot be extrapolated because the relationship

of the change in assumption to the change in fair value may not be linear. Also, the effect of a variation in a particular assumption on the fair value of the retained interests is calculated without changing any other assumption; generally, changes in one factor may result in changes in another, which may magnify or counteract the sensitivities.

The second table below summarizes certain cash flows received from securitizations in 2002 and 2001.

Sensitivity of key assumptions to adverse changes (1)

| | Impact on fair value | |
|--|----------------------|----------------------------|
| | Credit card loans | Residential mortgage loans |
| Fair value of retained interests | \$ 15.1 | \$ 94.6 |
| Weighted average remaining service life (in years) | .2 | 3.9 |
| Payment rate | 39.07% | 13.62% |
| Impact on fair value of 10% adverse change | \$ (1.0) | \$ (2.7) |
| Impact on fair value of 20% adverse change | (1.9) | (5.3) |
| Excess spread, net of credit losses | 5.92% | 1.19% |
| Impact on fair value of 10% adverse change | \$ (1.5) | \$ (9.5) |
| Impact on fair value of 20% adverse change | (3.1) | (18.9) |
| Expected credit losses | 1.68% | – |
| Impact on fair value of 10% adverse change | \$ (.5) | \$ – |
| Impact on fair value of 20% adverse change | (.9) | – |
| Discount rate | 12.50% | 4.55% |
| Impact on fair value of 10% adverse change | \$ (.1) | \$ (.3) |
| Impact on fair value of 20% adverse change | (.1) | (.6) |

(1) All rates are annualized except for credit card loans payment rate, which is monthly.

Cash flows from securitizations

| | 2002 | | 2001 | |
|---|-------------------|----------------------------|-------------------|----------------------------|
| | Credit card loans | Residential mortgage loans | Credit card loans | Residential mortgage loans |
| Proceeds from new securitizations | \$ – | \$ 1,691 | \$ 1,000 | \$ 720 |
| Proceeds reinvested in revolving securitizations | 8,512 | 303 | 6,972 | 13 |
| Cash flows from retained interests in securitizations | 64 | 15 | 60 | 10 |

NOTE 8 Premises and equipment

| | 2002 | | | 2001 |
|---|----------|--------------------------|----------------|----------------|
| | Cost | Accumulated depreciation | Net book value | Net book value |
| Land | \$ 172 | \$ — | \$ 172 | \$ 123 |
| Buildings | 606 | 287 | 319 | 335 |
| Computer equipment | 1,654 | 1,198 | 456 | 441 |
| Furniture, fixtures and other equipment | 976 | 650 | 326 | 313 |
| Leasehold improvements | 901 | 521 | 380 | 390 |
| | \$ 4,309 | \$ 2,656 | \$ 1,653 | \$ 1,602 |

The depreciation and amortization expense for premises and equipment amounted to \$407 million and \$389 million in 2002 and 2001, respectively.

NOTE 9 Other assets

| | 2002 | 2001 |
|--|-----------|-----------|
| Receivable from brokers, dealers and clients | \$ 3,229 | \$ 3,505 |
| Accrued interest receivable | 1,319 | 1,759 |
| Net deferred income tax asset | 999 | 1,096 |
| Insurance-related assets (1) | 936 | 708 |
| Prepaid pension benefit cost (2) | 429 | 368 |
| Investment in associated corporations | 92 | 69 |
| Other | 4,109 | 4,430 |
| | \$ 11,113 | \$ 11,935 |

- (1) Insurance-related assets include, among other items, policy loan balances, premiums outstanding, amounts due from other insurers in respect of reinsurance contracts and pooling arrangements and deferred acquisition costs.
- (2) Prepaid pension benefit cost represents the cumulative excess of pension fund contributions over the amounts recorded as pension benefit expense.

NOTE 10 Deposits

| | 2002 | | | | 2001 |
|-----------------------------|------------|------------|------------|------------|------------|
| | Demand (1) | Notice (2) | Term (3) | Total | Total |
| Personal | \$ 10,735 | \$ 30,065 | \$ 61,092 | \$ 101,892 | \$ 101,381 |
| Business and government | 39,004 | 8,864 | 71,723 | 119,591 | 107,141 |
| Bank | 1,705 | 85 | 20,213 | 22,003 | 24,925 |
| | \$ 51,444 | \$ 39,014 | \$ 153,028 | \$ 243,486 | \$ 233,447 |
| Non-interest-bearing | | | | \$ 21,843 | \$ 20,501 |
| Canada | | | | | |
| United States | | | | 2,078 | 1,918 |
| Other International | | | | 891 | 543 |
| Interest-bearing | | | | 119,737 | 118,161 |
| Canada | | | | | |
| United States | | | | 35,320 | 24,825 |
| Other International | | | | 63,617 | 67,499 |
| | | | | \$ 243,486 | \$ 233,447 |

- (1) Deposits payable on demand include all deposits for which we do not have the right to notice of withdrawal. These deposits are for the most part, chequing accounts.
- (2) Deposits payable after notice include all deposits for which we can legally require notice of withdrawal. These deposits are for the most part, savings accounts.
- (3) Term deposits include deposits payable on a fixed date. These deposits include term deposits, guaranteed investment certificates and similar instruments. At October 31, 2002, the balance of term deposits also includes senior deposit notes we have issued to provide long-term funding of \$11.3 billion (2001 – \$10.7 billion) and other notes and similar instruments in bearer form we have issued of \$21.7 billion (2001 – \$18.5 billion).

NOTE 11 Other liabilities

| | 2002 | 2001 |
|--|------------------|------------------|
| Short-term borrowings of subsidiaries | \$ 10,173 | \$ 6,838 |
| Payable to brokers, dealers and clients | 3,630 | 3,202 |
| Insurance claims and policy benefit liabilities | 3,424 | 2,986 |
| Accrued interest payable | 1,399 | 2,114 |
| Accrued pension and other postretirement benefit expense (1) | 574 | 630 |
| Dividends payable | 289 | 273 |
| Other | 6,708 | 7,737 |
| | \$ 26,197 | \$ 23,780 |

(1) Accrued pension and other postretirement benefit expense represents the cumulative excess of pension and other postretirement benefit expense over pension fund contributions.

NOTE 12 Subordinated debentures

The debentures are unsecured obligations and are subordinated in right of payment to the claims of depositors and certain other creditors. All redemptions, cancellations and exchanges of subordinated debentures

are subject to the consent and approval of the Superintendent of Financial Institutions Canada.

| Maturity | Earliest par value redemption date | Interest rate | Denominated in foreign currency | 2002 | 2001 |
|--------------------|------------------------------------|---------------|---------------------------------|-----------------|-----------------|
| January 11, 2002 | | 11.00% | \$ | — | \$ 41 |
| March 1, 2002 | | 10.50% | | — | 60 |
| September 3, 2007 | (1) | 5.40% | | — | 400 |
| September 3, 2008 | September 3, 2003 (2) | 5.45% (3) | | 100 | 100 |
| March 15, 2009 | | 6.50% | US\$125 | 195 | 199 |
| April 12, 2009 | April 12, 2004 (2) | 5.40% (3) | | 350 | 350 |
| June 11, 2009 | June 11, 2004 (2) | 5.10% (3) | | 350 | 350 |
| July 7, 2009 | July 7, 2004 (2) | 6.05% (3) | | 175 | 175 |
| October 12, 2009 | October 12, 2004 (2) | 6.00% (3) | | 150 | 150 |
| August 15, 2010 | August 15, 2005 (2) | 6.40% (3) | | 700 | 700 |
| February 13, 2011 | February 13, 2006 (4) | 5.50% (3) | | 125 | 125 |
| April 26, 2011 | April 26, 2006 (5) | 8.20% (3) | | 100 | 100 |
| September 12, 2011 | September 12, 2006 (2) | 6.50% (3) | | 350 | 350 |
| October 24, 2011 | October 24, 2006 (6) | 6.75% (7) | US\$300 | 467 | 476 |
| November 8, 2011 | November 8, 2006 (8) | (9) | US\$400 | 625 | — |
| June 4, 2012 | June 4, 2007 (2) | 6.75% (3) | | 500 | 500 |
| January 22, 2013 | January 22, 2008 (10) | 6.10% (3) | | 500 | 500 |
| November 14, 2014 | | 10.00% | | 200 | 200 |
| January 25, 2015 | January 25, 2010 (11) | 7.10% (3) | | 500 | 500 |
| April 12, 2016 | April 12, 2011 (12) | 6.30% (3) | | 400 | 400 |
| June 8, 2023 | | 9.30% | | 110 | 110 |
| October 1, 2083 | (13) | (14) | | 250 | 250 |
| June 6, 2085 | (13) | (15) | US\$300 | 467 | 477 |
| | | | | \$ 6,614 | \$ 6,513 |

- (1) Redeemed on September 3, 2002 at par value.
- (2) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on Government of Canada bonds plus 5 basis points and (ii) par value, and thereafter at any time at par value.
- (3) Interest at stated interest rate until earliest par value redemption date, and thereafter at a rate of 1.00% above the 90-day Bankers' Acceptance rate.
- (4) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on Government of Canada bonds plus 8 basis points and (ii) par value, and thereafter at any time at par value.
- (5) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on Government of Canada bonds plus 10 basis points and (ii) par value, and thereafter at any time at par value.
- (6) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on U.S. Treasury notes plus 10 basis points and (ii) par value, and thereafter at any time at par value.
- (7) Interest at a rate of 6.75% until earliest par value redemption date, and thereafter at a rate of 1.00% above the U.S. dollar 6-month LIBOR.
- (8) Redeemable on the earliest par value redemption date at par value.
- (9) Interest at a rate of .50% above the U.S. dollar 3-month LIBOR until earliest par value redemption date, and thereafter at a rate of 1.50% above the U.S. dollar 3-month LIBOR.
- (10) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on Government of Canada bonds plus 18 basis points and (ii) par value, and thereafter at any time at par value.
- (11) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on Government of Canada bonds plus 12.5 basis points and (ii) par value, and thereafter at any time at par value.
- (12) Redeemable at any time prior to the earliest par value redemption date at the greater of (i) the fair value of the subordinated debentures based on the yield on Government of Canada bonds plus 22 basis points and (ii) par value, and thereafter at any time at par value.
- (13) Redeemable on any interest payment date at par value.
- (14) Interest at a rate of .40% above the 30-day Bankers' Acceptance rate.
- (15) Interest at a rate of .25% above the U.S. dollar 3-month LIMEAN. In the event of a reduction of the annual dividend we declare on our common shares, the interest payable on the debentures is reduced pro rata to the dividend reduction and the interest reduction is payable with the proceeds from the sale of newly issued common shares.

NOTE 12 Subordinated debentures (continued)**Maturity schedule**

The aggregate maturities of subordinated debentures, based on the maturity dates under the terms of issue, are as follows:

| | |
|--------------|-----------------|
| 2003 – 2007 | \$ – |
| 2008 to 2012 | 4,187 |
| Thereafter | 2,427 |
| | \$ 6,614 |

NOTE 13 Capital stock**Authorized capital stock**

Preferred – An unlimited number of First Preferred Shares and Second Preferred Shares without nominal or par value, issuable in series; the aggregate consideration for which all the First Preferred Shares and all the Second Preferred Shares that may be issued may not exceed \$10 billion and \$5 billion, respectively.

Common – An unlimited number of shares without nominal or par value may be issued.

Issued and outstanding capital stock

| | 2002 | | | 2001 | | | 2000 | | |
|--|-------------------------|-----------------|------------------------------|-------------------------|-----------------|------------------------------|-------------------------|-----------------|------------------------------|
| | Number of shares (000s) | Amount | Dividends declared per share | Number of shares (000s) | Amount | Dividends declared per share | Number of shares (000s) | Amount | Dividends declared per share |
| First Preferred | | | | | | | | | |
| Non-cumulative Series E (1) | – | \$ – | \$ 3.06 | 1,500 | \$ 150 | \$ 5.16 | 1,500 | \$ 150 | \$ 5.38 |
| Non-cumulative Series H (1) | – | – | – | – | – | 1.69 | 12,000 | 300 | 2.25 |
| US\$ Non-cumulative Series I (1) | – | – | US .02 | 8,000 | 318 | US 1.91 | 8,000 | 304 | US 1.91 |
| Non-cumulative Series J | 12,000 | 300 | 1.78 | 12,000 | 300 | 1.78 | 12,000 | 300 | 1.78 |
| US\$ Non-cumulative Series K | 10,000 | 389 | US 1.58 | 10,000 | 397 | US 1.58 | 10,000 | 381 | US 1.58 |
| Non-cumulative Series N | 12,000 | 300 | 1.18 | 12,000 | 300 | 1.18 | 12,000 | 300 | 1.18 |
| Non-cumulative Series O | 6,000 | 150 | 1.38 | 6,000 | 150 | 1.38 | 6,000 | 150 | 1.38 |
| US\$ Non-cumulative Series P | 4,000 | 156 | US 1.44 | 4,000 | 159 | US 1.44 | 4,000 | 152 | US 1.44 |
| Non-cumulative Series S | 10,000 | 250 | 1.53 | 10,000 | 250 | .65 | – | – | – |
| | | \$ 1,545 | | | \$ 2,024 | | | \$ 2,037 | |
| Common | | | | | | | | | |
| Balance at beginning of year | 674,021 | \$ 6,973 | | 602,398 | \$ 3,076 | | 617,768 | \$ 3,065 | |
| Issued | – | – | | 12,305 | 576 | | – | – | |
| Issued under the stock option plan (2) | 5,211 | 176 | | 2,819 | 81 | | 2,700 | 59 | |
| Issued on the acquisition of Centura Banks, Inc. | – | – | | 67,413 | 3,317 | | – | – | |
| Options granted on acquisition of Dain Rauscher Corporation | – | 14 | | – | 33 | | – | – | |
| Issued on the acquisition of Richardson Greenshields Limited (3) | 318 | 15 | | 13 | 2 | | 1,667 | 50 | |
| Renounced stock appreciation rights, net of related income taxes | – | 31 | | – | – | | – | – | |
| Purchased for cancellation (4) | (14,293) | (152) | | (10,927) | (112) | | (19,737) | (98) | |
| Balance at end of year | 665,257 | \$ 7,057 | \$ 1.51 | 674,021 | \$ 6,973 | \$ 1.38 | 602,398 | \$ 3,076 | \$ 1.14 |

- (1) On November 26, 2001 and October 11, 2002, we redeemed First Preferred Shares Series I and E, respectively. On August 24, 2001, we redeemed First Preferred Shares Series H.
- (2) Includes the exercise of stock options from tandem stock appreciation rights awards, resulting in a reversal of the accrued liability, net of related income taxes, of \$9 million.
- (3) During the year we exchanged nil (2001 – 36,527; 2000 – 4,701) Class B shares and 1,846,897 (2001 – 77,956; 2000 – 8,008,712) Class C shares issued by our wholly owned subsidiary, Royal Bank DS Holding Inc., on the acquisition of Richardson Greenshields Limited for 318,154 (2001 – 13,621; 2000 – 1,667,334) common shares.
- (4) Commencing in June 2001, pursuant to a one-year normal course issuer bid, we repurchased through the facilities of the Toronto and Montreal Stock Exchanges 15,401,100 common shares at an average price of \$49.32 per share. Under this bid, 10,927,200 common shares were repurchased during fiscal 2001 at a cost of \$509 million and 4,473,900 common shares were repurchased during fiscal 2002 at a cost of \$251 million. On June 24, 2002, we renewed our one-year normal course issuer bid to purchase for cancellation, up to 20 million of our common shares, representing approximately 3% of our outstanding common shares. Under this renewed bid, 9,818,900 common shares were purchased, at an average cost of \$52.27 per share, for \$513 million. During fiscal 2002, a total of 14,292,800 common shares were repurchased for \$764 million at an average cost of \$53.45 per share.

NOTE 13 Capital stock (continued)**Terms of preferred shares**

| | Dividend per share (1) | Redemption date (2) | Redemption price (3) | Conversion dates | |
|------------------------------|---------------------------|------------------------|-------------------------|---------------------------------------|------------------------------------|
| | | | | At the option of the bank (2), (4) | At the option of the holder (5) |
| First Preferred | | | | | |
| Non-cumulative Series J | 0.443750 | May 24, 2003 | 25.00 | May 24, 2003 | November 24, 2003 |
| US\$ Non-cumulative Series K | US 0.393750 | May 24, 2003 | US 25.00 | May 24, 2003 | November 24, 2003 |
| Non-cumulative Series N | 0.293750 | August 24, 2003 | 26.00 | August 24, 2003 | August 24, 2008 |
| Non-cumulative Series O | 0.343750 | August 24, 2004 | 26.00 | August 24, 2004 | Not convertible |
| US\$ Non-cumulative Series P | US 0.359375 | August 24, 2004 | US 26.00 | August 24, 2004 | Not convertible |
| Non-cumulative Series S | 0.38125 | August 24, 2006 | 26.00 | August 24, 2006 | Not convertible |

- (1) Non-cumulative preferential dividends on Series J, K, N, O, P and S are payable quarterly, as and when declared by the Board of Directors, on or about the 24th day of February, May, August and November.
- (2) Subject to the consent of the Superintendent of Financial Institutions Canada and the requirements of the *Bank Act*, we may, on or after the dates specified above, redeem First Preferred Shares. These may be redeemed (i) for cash, in the case of First Preferred Shares Series J and K equal to the redemption price as stated above, in the case of Series N at a price per share of \$26, if redeemed during the 12 months commencing August 24, 2003, and decreasing by \$0.25 each 12-month period thereafter to a price per share of \$25 if redeemed on or after August 24, 2007, and in the case of Series O and P at a price per share of \$26 if redeemed during the 12 months commencing August 24, 2004, and decreasing by \$0.25 each 12-month period thereafter to a price per share of \$25 if redeemed on or after August 24, 2008, and in the case of Series S at a price per share of \$26 if redeemed during the 12 months commencing August 26, 2006, and decreasing by \$0.25 each 12-month period thereafter to a price per share of \$25 if redeemed on or after August 24, 2010, or (ii) by conversion, in the case of Series J and K into that number of common shares determined by dividing the then-applicable redemption price by the greater of \$2.50 and 95% of the weighted average trading price of common shares at such time.
- (3) Subject to the consent of the Superintendent of Financial Institutions Canada and the requirements of the *Bank Act*, we may purchase First Preferred Shares for cancellation at a purchase price, in the case of the Series J and K not exceeding the then-applicable redemption price specified above plus all declared and unpaid dividends, and, in the case of the Series N, O, P and S at the lowest price or prices at which, in the opinion of the Board of Directors, such shares are obtainable.
- (4) Subject to the approval of the Toronto Stock Exchange, we may, on or after the dates specified above, convert First Preferred Shares Series N, O, P and S into our common shares. First Preferred Shares may be converted into that number of common shares determined by dividing the then-applicable redemption price by the greater of \$2.50 and 95% of the weighted average trading price of common shares at such time.
- (5) Subject to our right to redeem or to find substitute purchasers, the holder may, on or after the dates specified above, convert First Preferred Shares into our common shares. Series J, K and N may be converted, quarterly, into that number of common shares determined by dividing the then-applicable redemption price by the greater of \$2.50 and 95% of the weighted average trading price of common shares at such time.

Restrictions on the payment of dividends

We are prohibited by the *Bank Act* (Canada) from declaring any dividends on our preferred or common shares when we are, or would be placed as a result of the declaration, in contravention of the capital adequacy and liquidity regulations or any regulatory directives issued under the act. We may not pay dividends on our common shares at any time unless all dividends to which preferred shareholders are then entitled have been declared and paid or set apart for payment.

In addition, we may not declare or pay a dividend without the approval of the Superintendent of Financial Institutions Canada (OSFI) if, on the day the dividend is declared, the total of all dividends in that year would exceed the aggregate of our net income up to that day and of our retained net income for the preceding two years.

We have agreed that if RBC Capital Trust (a closed-end trust, which is a subsidiary) fails to pay any required distribution on its capital trust securities, we will not declare dividends of any kind on any of our preferred or common shares.

Currently, these limitations do not restrict the payment of dividends on our preferred or common shares.

Regulatory capital

We are subject to the regulatory capital requirements defined by OSFI, which includes the use of Canadian GAAP. Two measures of capital

strength established by OSFI, based on standards issued by the Bank for International Settlements (BIS), are risk-adjusted capital ratios and the assets-to-capital multiple.

OSFI requires Canadian banks to maintain a minimum Tier 1 and Total capital ratio of 4% and 8%, respectively. However, OSFI has also formally established risk-based capital targets for deposit-taking institutions in Canada. These targets are a Tier 1 capital ratio of at least 7% and a Total capital ratio of at least 10%. At October 31, 2002, our Tier 1 and Total capital ratios were 9.3% and 12.7%, respectively (2001 – 8.7% and 11.8%, respectively).

In the evaluation of our assets-to-capital multiple, OSFI specifies that total assets, including specified off-balance sheet financial instruments, should be no greater than 23 times Total capital. At October 31, 2002, our assets-to-capital multiple was 17.3 times (2001 – 17.2 times).

Other

In 2000, we entered into an agreement with a AAA rated reinsurer, which requires the reinsurer to purchase up to \$200 million of non-cumulative first preferred shares at the October 27, 2000 market price should the general allowance for credit losses (allocated general and unallocated) be drawn down below a certain level. During the year, the reinsurer was downgraded from AAA. Based on this development and an internal review by management, the agreement was not renewed.

NOTE 14 Income taxes

| | 2002 | 2001 | 2000 |
|--|-----------------|---------------|-----------------|
| Provision for income tax in income | | | |
| Current | | | |
| Canada – Federal | \$ 703 | \$ 845 | \$ 799 |
| Provincial | 272 | 360 | 349 |
| International | 155 | 103 | 258 |
| | 1,130 | 1,308 | 1,406 |
| Deferred | | | |
| Canada – Federal | 167 | 16 | 60 |
| Provincial | 57 | 1 | 20 |
| International | 11 | 15 | (41) |
| | 235 | 32 | 39 |
| | 1,365 | 1,340 | 1,445 |
| Income tax expense (benefit) in shareholders' equity | | | |
| Unrealized foreign currency translation gains and losses, net of hedging activities | 100 | (487) | (37) |
| Stock appreciation rights | 25 | – | – |
| Cumulative effect of initial adoption of <i>Employee Future Benefits</i> accounting standard | – | (157) | – |
| | 125 | (644) | (37) |
| Total income taxes | \$ 1,490 | \$ 696 | \$ 1,408 |

Deferred income taxes (temporary differences)

| | 2002 | 2001 | 2000 |
|--------------------------------------|---------------|-----------------|---------------|
| Deferred income tax asset (1) | | | |
| Allowance for credit losses | \$ 512 | \$ 582 | \$ 514 |
| Deferred compensation | 339 | 190 | 78 |
| Pension related | 43 | 93 | – |
| Tax loss carryforwards | 22 | 84 | 72 |
| Premises and equipment | – | – | 83 |
| Deferred income | 60 | 61 | 81 |
| Other | 259 | 399 | 223 |
| | 1,235 | 1,409 | 1,051 |
| Deferred income tax liability | | | |
| Premises and equipment | (9) | (91) | – |
| Deferred expense | (77) | (88) | (59) |
| Pension related | – | – | (119) |
| Other | (150) | (134) | (77) |
| | (236) | (313) | (255) |
| Net deferred income tax asset | \$ 999 | \$ 1,096 | \$ 796 |

(1) We have determined that it is more likely than not that the deferred income tax asset will be realized through a combination of future reversals of temporary differences and taxable income.

Reconciliation to statutory tax rate

| | 2002 | | 2001 | | 2000 | |
|--|----------|-------|----------|-------|----------|-------|
| Income taxes at Canadian statutory tax rate | \$ 1,630 | 38.5% | \$ 1,601 | 41.5% | \$ 1,600 | 42.8% |
| Increase (decrease) in income taxes resulting from | | | | | | |
| Lower average tax rate applicable to subsidiaries | (276) | (6.5) | (253) | (6.5) | (311) | (8.3) |
| Tax-exempt income from securities | (7) | (.2) | (7) | (.2) | (7) | (.2) |
| Tax rate change | 33 | .8 | 63 | 1.6 | 36 | 1.0 |
| Other | (15) | (.4) | (64) | (1.7) | 127 | 3.3 |
| Income taxes reported in income/effective tax rate | \$ 1,365 | 32.2% | \$ 1,340 | 34.7% | \$ 1,445 | 38.6% |

International earnings of certain subsidiaries would be taxed only upon their repatriation to Canada. We have not recognized a deferred tax liability for these undistributed earnings as we do not currently expect them to be repatriated. Taxes that would be payable if all foreign subsidiaries'

accumulated unremitted earnings were repatriated are estimated at \$841 million as at October 31, 2002 (2001 – \$772 million; 2000 – \$737 million).

NOTE 15 Pensions and other postretirement benefits

We sponsor a number of defined benefit and defined contribution plans providing pension and other postretirement benefits to eligible employees.

The following tables present information related to our benefit plans, including amounts recorded on the Consolidated balance sheet and the components of net benefit expense:

Plan assets, benefit obligation and funded status

| | Pension plans (1) | | Other postretirement plans (2) | |
|---|-------------------|----------|--------------------------------|----------|
| | 2002 | 2001 | 2002 | 2001 |
| Change in fair value of plan assets (3) | | | | |
| Fair value of plan assets, October 1 | \$ 4,049 | \$ 4,519 | \$ 1 | \$ 67 |
| Actual return on plan assets | (133) | (476) | - | 7 |
| Company contributions | 99 | 20 | 23 | 21 |
| Plan participant contributions | 19 | 18 | 1 | - |
| Benefits paid | (258) | (251) | (25) | (22) |
| Plan settlements | (52) | - | - | (72) |
| Business acquisitions | - | 63 | - | - |
| Change in foreign currency exchange rate | 17 | 12 | - | - |
| Transfers from other plans | 6 | 144 | - | - |
| Fair value of plan assets, September 30 | \$ 3,747 | \$ 4,049 | \$ - | \$ 1 |
| Change in benefit obligation | | | | |
| Benefit obligation, October 1 | \$ 4,044 | \$ 3,710 | \$ 693 | \$ 609 |
| Service cost | 113 | 104 | 22 | 64 |
| Interest cost | 297 | 268 | 51 | 49 |
| Plan participant contributions | 19 | 18 | 1 | - |
| Actuarial loss | 280 | 55 | 318 | 19 |
| Benefits paid | (258) | (251) | (25) | (22) |
| Transfers from other plans | 3 | - | - | - |
| Plan amendments and curtailments | 59 | 31 | 7 | - |
| Plan settlements | - | - | - | (72) |
| Business acquisitions | 2 | 117 | - | 35 |
| Change in foreign currency exchange rate | 31 | (9) | - | - |
| Changes in assumptions | - | 1 | - | 11 |
| Benefit obligation, September 30 | \$ 4,590 | \$ 4,044 | \$ 1,067 | \$ 693 |
| Funded status | | | | |
| (Deficit) excess of plan assets over benefit obligation | \$ (843) | \$ 5 | \$ (1,067) | \$ (692) |
| Unrecognized net actuarial loss | 792 | 32 | 360 | 42 |
| Unrecognized transition (asset) obligation | (26) | (24) | 190 | 207 |
| Unrecognized prior service cost | 211 | 205 | 13 | 10 |
| Contributions between September 30 and October 31 | 222 | - | 3 | - |
| Other | (1) | (48) | 1 | 1 |
| Prepaid asset (accrued liability) as at October 31 | \$ 355 | \$ 170 | \$ (500) | \$ (432) |
| Weighted average assumptions | | | | |
| Discount rate | 6.75% | 7.00% | 7.00% | 7.25% |
| Assumed long-term rate of return on plan assets | 7.00% | 7.00% | 4.75% | 4.75% |
| Rate of increase in future compensation | 4.00% | 4.40% | 4.40% | 4.40% |

Pension benefit expense (4)

| | 2002 | 2001 | 2000 |
|--------------------------------------|--------|--------|-------|
| Service cost | \$ 113 | \$ 104 | \$ 98 |
| Interest cost | 297 | 268 | 254 |
| Expected return on plan assets | (300) | (306) | (291) |
| Amortization of transition asset | (2) | (2) | (2) |
| Amortization of prior service cost | 32 | 17 | 22 |
| Recognized net actuarial gain | (27) | (45) | (41) |
| Settlement loss | 52 | - | - |
| Other | (45) | (14) | 19 |
| Defined benefit pension expense | 120 | 22 | 59 |
| Defined contribution pension expense | 61 | 30 | 6 |
| Pension benefit expense | \$ 181 | \$ 52 | \$ 65 |

Other postretirement benefit expense (2)

| | 2002 | 2001 | 2000 |
|---------------------------------------|-------|--------|-------|
| Service cost | \$ 22 | \$ 64 | \$ 17 |
| Interest cost | 51 | 49 | 42 |
| Expected return on plan assets | - | (1) | (3) |
| Amortization of transition obligation | 17 | 17 | 17 |
| Other | 2 | 2 | - |
| Other postretirement benefit expense | \$ 92 | \$ 131 | \$ 73 |

2002 sensitivity of key assumptions

| | Change in obligation | Change in expense |
|---|----------------------|-------------------|
| Pensions | | |
| Impact of .25% change in discount rate assumption | \$ 126 | \$ 16 |
| Impact of .25% change in rate of increase in future compensation assumption | 29 | 2 |
| Impact of .25% change in the long-term rate of return on plan assets assumption | - | 10 |
| Postretirement | | |
| Impact of .25% change in discount rate assumption | \$ 48 | \$ 3 |
| Impact of .25% change in rate of increase in future compensation assumption | 4 | 1 |

- (1) Included in these amounts are \$3,239 million (2001 – \$266 million) of plan assets and \$4,131 million (2001 – \$567 million) of benefit obligations for plans that are not fully funded.
- (2) Includes postretirement health, dental and life insurance. The assumed health care cost trend rates for the next year used to measure the expected cost of benefits covered for the postretirement health and life plans were 8% for medical and 5% for dental, decreasing to an ultimate rate of 4% in 2009. A one percentage point increase in assumed health care cost trend rates would have increased the service and interest costs and obligation by \$12 million and \$142 million, respectively. A one percentage point decrease in assumed health care cost trends would have lowered the service and interest costs and the obligation by \$8 million and \$112 million, respectively.
- (3) Plan assets includes 818,597 (2001 – 886,384) of Royal Bank common shares having a fair value of \$43 million (2001 – \$43 million). In addition, dividends amounting to \$1 million (2001 – \$1 million) were received on Royal Bank common shares held in the plan assets during the year.
- (4) Discount rate assumption of 7.00% (2001 – 7.00%; 2000 – 7.25%) was used to determine pension benefit expense.

NOTE 16 Stock-based compensation**Stock option plans**

We have two stock option plans – one for certain key employees and one for non-employee directors. Under these plans, options are periodically granted to purchase common shares at prices not less than the market price of such shares on the day of grant. The options vest over a 4-year period for employees and immediately for directors and are exercisable for a period not exceeding 10 years from the grant date.

For options issued prior to October 31, 2002 that were not accompanied by tandem stock appreciation rights (SARs), no compensation expense was recognized as the option's exercise price was not less than the market price of the underlying stock on the day of grant. When the options are exercised, the proceeds received are credited to common shares.

Between November 29, 1999 and June 5, 2001, grants of options under the employee stock option plan were accompanied by tandem SARs.

With SARs, participants could choose to exercise a SAR instead of the corresponding option. In such cases, the participants received a cash payment equal to the difference between the closing price of common shares on the day immediately preceding the day of exercise and the exercise price of the option. The compensation expense for these grants, which is amortized over the associated option's vesting period, was \$44 million for the year ended October 31, 2002 (2001 – \$23 million; 2000 – \$52 million).

During the last quarter of 2002, certain executive participants voluntarily renounced their SARs while retaining the corresponding options. At the time of renouncement, the compensation cost was fixed and the accrued liability of \$51 million was transferred to equity.

Stock options

| | 2002 | | 2001 | | 2000 | |
|----------------------------------|--------------------------|---------------------------------|--------------------------|---------------------------------|--------------------------|---------------------------------|
| | Number of options (000s) | Weighted average exercise price | Number of options (000s) | Weighted average exercise price | Number of options (000s) | Weighted average exercise price |
| Outstanding at beginning of year | 30,158 | \$ 36.84 | 25,880 | \$ 33.61 | 20,966 | \$ 32.42 |
| Granted | 4,215 | 49.12 | 7,949 | 44.46 | 8,286 | 33.09 |
| Exercised – Common shares | (5,211) | 32.07 | (2,819) | 28.77 | (2,700) | 22.05 |
| – SARs | (291) | 34.01 | (259) | 33.55 | – | – |
| Cancelled | (392) | 38.37 | (593) | 37.82 | (672) | 36.10 |
| Outstanding at end of year | 28,479 | \$ 39.54 | 30,158 | \$ 36.84 | 25,880 | \$ 33.61 |
| Exercisable at end of year | 14,050 | \$ 36.07 | 12,895 | \$ 32.62 | 8,881 | \$ 30.29 |
| Available for grant | 16,105 | | 20,289 | | 25,849 | |

Range of exercise prices

| | Options outstanding | | | Options exercisable | |
|-----------------|---------------------------|---------------------------------|---|---------------------------|---------------------------------|
| | Number outstanding (000s) | Weighted average exercise price | Weighted average remaining contractual life | Number exercisable (000s) | Weighted average exercise price |
| \$14.46–\$15.68 | 587 | \$ 15.57 | 3.9 | 587 | \$ 15.57 |
| \$24.80–\$28.25 | 2,816 | 26.19 | 6.9 | 2,401 | 25.85 |
| \$30.00–\$39.64 | 15,175 | 36.68 | 7.1 | 9,595 | 37.90 |
| \$43.59–\$52.19 | 9,901 | 49.15 | 9.4 | 1,467 | 49.04 |
| Total | 28,479 | \$ 39.54 | 7.8 | 14,050 | \$ 36.07 |

Fair value method

CICA 3870, *Stock-based Compensation and Other Stock-based Payments*, recommends the recognition of an expense for option awards using the fair value method of accounting. It permits the use of other methods, including the intrinsic value based method, provided pro forma disclosures of net income and earnings per share applying the fair value method are made. We will be adopting the recommendations of CICA 3870

prospectively for new awards granted after November 1, 2002. The impact is an estimated charge to earnings of \$6 million for the year ended October 31, 2003.

We have provided pro forma disclosures, which demonstrate the effect as if we had adopted the recommended recognition provisions of CICA 3870 in 2002, 2001 and 2000 as indicated below:

Pro forma net income and earnings per share

| | 2002 | As reported | | Pro forma (1) | | |
|----------------------------|----------|-------------|----------|---------------|----------|----------|
| | | 2001 | 2000 | 2002 | 2001 | 2000 |
| Net income | \$ 2,762 | \$ 2,411 | \$ 2,274 | \$ 2,730 | \$ 2,375 | \$ 2,230 |
| Earnings per share | 3.96 | 3.55 | 3.53 | 3.91 | 3.49 | 3.46 |
| Diluted earnings per share | 3.93 | 3.52 | 3.51 | 3.89 | 3.47 | 3.44 |

(1) Compensation expense under the fair value based method is recognized over the vesting period of the related stock options. Accordingly, the pro forma results of applying this method may not be indicative of future amounts.

In determining the pro forma disclosures above, the fair value of options granted during 2002 was estimated on the date of grant using an option pricing model with the following assumptions: (i) risk-free interest rate of 4.89% (2001 – 5.86%, 2000 – 6.04%), (ii) expected option life of

6 years (2001; 2000 – 10 years), (iii) expected volatility of 20% (2001 – 24%; 2000 – 22%) and (iv) expected dividends of 2.9% (2001 – 2.67%; 2000 – 2.60%). The fair value of each option granted was \$10.02 (2001 – \$14.78; 2000 – \$10.26).

NOTE 16 Stock-based compensation (continued)**Employee share ownership plans**

We offer many employees an opportunity to own stock through RBC savings and share ownership plans. Under these plans, the employee can generally contribute between 1% and 10% of their annual salary or benefit base for commissioned employees. For each contribution between 1% and 6%, we will match 50% of the employee contributions in common shares. For the RBC Dominion Securities Savings Plan our maximum annual contribution is \$4,500 per employee. For the RBC UK Share Incentive Plan our maximum annual contribution is £1,500 per employee. We contributed \$49 million (2001 – \$47 million; 2000 – \$45 million), under the terms of these plans, towards the purchase of common shares. As at October 31, 2002, an aggregate of 17,397,119 common shares were held under these plans.

Deferred share and other plans

We offer deferred share unit plans to executives and non-employee directors. Under these plans, each executive or director may choose to receive all or a percentage of their annual incentive bonus or directors fee in the form of deferred share units (DSUs). The executives or directors must elect to participate in the plan prior to the beginning of the fiscal year. DSUs earn dividend equivalents in the form of additional DSUs at the same rate as dividends on common shares. The participant is not allowed to convert the DSUs until retirement, permanent disability or termination of employment/directorship. The cash value of the DSUs is equivalent to the market value of common shares when conversion takes place. The value of the DSUs as at October 31, 2002, was \$73 million (2001 – \$52 million; 2000 – \$26 million). The share appreciation and dividend-related compensation expense recorded for the year ended October 31, 2002 in respect of these plans was \$16 million (2001 – \$8 million, 2000 – \$7 million).

We have a deferred bonus plan for certain key employees within RBC Capital Markets. Under this plan, a percentage of each employee's annual incentive bonus is deferred and accumulates dividend equivalents at the same rate as dividends on common shares. The employee will receive the deferred bonus in equal amounts paid within 90 days of the following 3 year-end dates. The value of the deferred bonus paid will be equivalent to the original deferred bonus adjusted for dividends and changes in the market value of common shares at the time the bonus is paid. The value of the deferred bonus as at October 31, 2002, was \$187 million (2001 – \$128 million; 2000 – \$89 million). The share appreciation and dividend-related compensation expense for the year ended October 31, 2002 in respect of this plan was \$20 million (2001 – \$5 million recovery; 2000 – \$10 million).

We offer deferred share plans to certain key employees within RBC Investments with various vesting periods up to a maximum of five years. Awards under some of these plans may be deferred in the form of common shares, which are held in trust, or DSUs. The participant is not allowed to convert the DSU until retirement, permanent disability, or termination of employment. The cash value of DSUs is equivalent to the market value of common shares when conversion takes place. Certain plans award share units that track the value of common shares with pay-out in cash at the end of a maximum five-year term. The value of

deferred shares held in trust as at October 31, 2002, was \$34 million (2001 – \$14 million). The value of the various share units as at October 31, 2002, was \$10 million (2001 – \$4 million). The stock-based compensation expense recorded for the year ended October 31, 2002, in respect of these plans, was \$32 million (2001 – \$16 million; 2000 – \$14 million).

We offer a performance deferred share plan to certain key employees. The performance deferred share award is made up of 50% regular shares and 50% performance shares all of which vest at the end of 3 years. At the time the shares vest, the performance shares can be increased or decreased by 50% depending on our total shareholder return compared to 15 North American financial institutions. Compensation expense of \$11 million was recognized for the year ended October 31, 2002 in respect of this award. The value of common shares held in trust as at October 31, 2002, was \$34 million.

We offer a mid-term compensation plan to certain senior executive officers. Awards under this program are converted into share units equivalent to common shares. The share units vest over a three-year period in equal installments of one-third per year. The units have a value equal to the market value of common shares on each vesting date and are paid in either cash or common shares at our option. The value of the share units as at October 31, 2002 was \$16 million (2001 – \$21 million). The compensation expense recorded for the year ended October 31, 2002 in respect of this plan was \$12 million (2001 – \$8 million).

Dain Rauscher maintains a non-qualified deferred compensation plan for key employees under an arrangement called the wealth accumulation plan. This plan allows eligible employees to make deferrals of their annual income and allocate the deferrals among various fund choices, which include an RBC share unit fund that tracks the value of our common shares. Certain deferrals may also be eligible for matching contributions from us. All matching contributions are allocated to the RBC share unit fund. The compensation expense recorded for the year ended October 31, 2002, in respect of the matching contributions, was \$12 million (2001 – \$7 million). The value of the RBC share units held under the plan as at October 31 2002, was \$70 million (2001 – \$7 million).

For other stock-based plans, compensation expense of \$19 million was recognized for the year ended October 31, 2002 (2001 – \$14 million; 2000 – \$1 million). The value of the share units and shares held under these plans as at October 31, 2002 was \$10 million (2001 – \$3 million; 2000 – \$1 million).

Retention plan

On the acquisition of Dain Rauscher, certain key employees of Dain Rauscher were offered retention units awards totalling \$318 million in award value to be paid out evenly over expected service periods of between three and four years. Payments to participants of the plan are based on the market value of common shares on the vesting date. The compensation expense recorded for the year ended October 31, 2002 in respect of this plan was \$92 million (2001 – \$143 million). The liability under this plan was \$151 million as at October 31, 2002 (2001 – \$135 million).

NOTE 17 Earnings per share

| | 2002 | 2001 | 2000 |
|--|----------|----------|----------|
| Earnings per share | | | |
| Net income | \$ 2,762 | \$ 2,411 | \$ 2,274 |
| Preferred share dividends | (98) | (135) | (134) |
| Net income available to common shareholders | \$ 2,664 | \$ 2,276 | \$ 2,140 |
| Average number of common shares (in thousands) | 672,571 | 641,516 | 606,389 |
| | \$ 3.96 | \$ 3.55 | \$ 3.53 |
| Diluted earnings per share | | | |
| Net income available to common shareholders | \$ 2,664 | \$ 2,276 | \$ 2,140 |
| Effect of assumed conversions (1) | — | 1 | 2 |
| Net income adjusted for diluted computation | \$ 2,664 | \$ 2,277 | \$ 2,142 |
| Average number of common shares (in thousands) | 672,571 | 641,516 | 606,389 |
| Convertible Class B and C shares (1) | 14 | 363 | 736 |
| Stock options (2) | 5,535 | 5,337 | 2,740 |
| Average number of diluted common shares (in thousands) | 678,120 | 647,216 | 609,865 |
| | \$ 3.93 | \$ 3.52 | \$ 3.51 |

- (1) The convertible shares included the Class B and C shares issued by our wholly owned subsidiary Royal Bank DS Holding Inc., on the acquisition of Richardson Greenshields Limited on November 1, 1996. The outstanding Class B shares were all exchanged into Royal Bank of Canada common shares in 2001 and the remaining Class C shares were exchanged for common shares on November 9, 2001. The price of the Class C shares was determined based on our average common share price during the 20 days prior to the date the exchange was made. During the year we exchanged nil (2001 – 36,527; 2000 – 4,701) Class B shares and 1,846,897 (2001 – 77,956; 2000 – 8,008,712) Class C shares for 318,154 (2001 – 13,621; 2000 – 1,667,334) common shares.
- (2) The dilutive effect of stock options was calculated using the treasury stock method. This method calculates the number of incremental shares by assuming the outstanding stock options are (i) exercised and (ii) then reduced by the number of shares assumed to be repurchased from the issuance proceeds, using the average market price of our common shares for the period. Excluded from the calculation of diluted earnings per share were average options outstanding of 9,761 with an exercise price of \$53.76 (2001 – 7,862 at \$50.72; 1,956 at \$49.03; 2000 – 6,153,507 at \$39.64; 6,589,464 at \$39.01; 2,639 at \$38.22; and 393 at \$43.59) as the options' exercise price was greater than the average market price of our common shares.

NOTE 18 Commitments and contingencies**Financial instruments with contractual amounts representing credit risk**

The primary purpose of these commitments is to ensure that funds are available to a client as required. Our policy for requiring collateral security with respect to these instruments and the types of collateral security held is generally the same as for loans.

Guarantees and standby letters of credit, which represent irrevocable assurances that we will make payments in the event that a client cannot meet its obligations to third parties, carry the same credit risk as loans.

Documentary and commercial letters of credit, which are written undertakings by us on behalf of a client authorizing a third party to draw drafts on us up to a stipulated amount under specific terms and conditions, are collateralized by the underlying shipment of goods to which they relate.

In securities lending transactions, we act as an agent for the owner of a security, who agrees to lend the security to a borrower for a fee, under the terms of a pre-arranged contract. The borrower must fully collateralize the security loan at all times.

Commitments to extend credit represent unused portions of authorizations to extend credit in the form of loans, bankers' acceptances, guarantees or letters of credit.

Uncommitted amounts represent an amount for which we retain the option to extend credit to a borrower.

A note issuance facility represents an underwriting agreement that enables a borrower to issue short-term debt securities. A revolving underwriting facility represents a renewable note issuance facility that can be accessed for a specified period of time.

Financial instruments with contractual amounts representing credit risk

| | 2002 | 2001 |
|---|------------|------------|
| Guarantees and standby letters of credit | \$ 13,610 | \$ 13,391 |
| Documentary and commercial letters of credit | 772 | 750 |
| Securities lending | 23,967 | 21,377 |
| Commitments to extend credit | | |
| Original term to maturity of 1 year or less | 40,931 | 44,179 |
| Original term to maturity of more than 1 year | 34,115 | 39,960 |
| Uncommitted amounts | 45,978 | 53,750 |
| Note issuance/revolving underwriting facilities | 23 | 132 |
| | \$ 159,396 | \$ 173,539 |

NOTE 18 Commitments and contingencies (continued)**Lease commitments**

Minimum future rental commitments for premises and equipment under long-term non-cancellable leases for the next five years and thereafter are shown below.

Lease commitments

| | |
|--------------|-----------------|
| 2003 | \$ 364 |
| 2004 | 330 |
| 2005 | 300 |
| 2006 | 267 |
| 2007 | 203 |
| Thereafter | 754 |
| Total | \$ 2,218 |

Litigation

On June 21, 2002, a week before it was due to pay Royal Bank of Canada US\$517 million plus interest under the terms of a total return swap, which is recorded in Other assets, Cooperatieve Centrale Raiffeisen-Boerenleenbank B.A. (Rabobank) initiated an action against us in New York state court in an effort to nullify its obligation under the swap. On June 24, 2002, we instituted proceedings against Rabobank in the High Court in London, alleging that Rabobank had repudiated its obligation under the swap. On July 31, 2002, we filed a motion to dismiss

or stay Rabobank's New York lawsuit. Rabobank filed, on September 27, 2002, an application to stay our claim with the High Court in London. Both our motion to stay or dismiss and Rabobank's application to stay are proceeding and the matter of forum is expected to be considered by both courts in the near future. Management expects to recover this amount in its entirety and accordingly a provision for loss has not been recorded.

Various other legal proceedings are pending that challenge certain of our practices or actions. Many of these proceedings are loan-related and are in reaction to steps taken by us and our subsidiaries to collect delinquent loans and enforce rights in collateral securing such loans. Management considers that the aggregate liability resulting from these proceedings will not be material.

Pledged assets

In the ordinary course of business we accept collateral, generally under reverse repurchase and securities borrowing agreements. The fair value of collateral accepted that can be sold or repledged by us totalled \$55.9 billion (2001 – \$52.9 billion). Of this collateral, \$36.4 billion (2001 – \$41.9 billion) has been sold or repledged, generally as collateral under repurchase agreements or to cover short sales. Details of assets pledged against liabilities, including amounts that cannot be sold or repledged by the secured party, are shown below:

Pledged assets

| | 2002 | 2001 |
|--|------------------|------------------|
| Assets pledged to: | | |
| Foreign governments and central banks | \$ 1,418 | \$ 113 |
| Clearing systems, payment systems and depositories | 1,075 | 2,470 |
| Assets pledged in relation to: | | |
| Derivative transactions | 1,828 | 830 |
| Securities borrowing and lending | 20,840 | 16,413 |
| Obligations related to securities sold under repurchase agreements | 21,109 | 20,855 |
| Other | 3,389 | 6,095 |
| Total | \$ 49,659 | \$ 46,776 |

NOTE 19 Derivative financial instruments

Derivative financial instruments are financial contracts whose value is derived from an underlying interest rate, foreign exchange rate, equity or commodity instrument or index.

Derivative product types

We use the following derivative financial instruments for both trading and non-trading purposes.

Swaps are transactions in which two parties exchange cash flows on a specified notional amount for a predetermined period. For interest rate swaps, fixed and floating interest payments are exchanged based on a notional amount. Cross currency swaps involve the exchange of fixed or floating interest payments in one currency for the receipt of fixed or floating interest payments in another currency. Cross currency interest rate swaps involve the exchange of both interest and principal amounts in two different currencies.

Forwards and futures are contractual obligations to buy or sell a financial instrument on a future date at a specified price. Forward contracts are effectively tailor-made agreements that are transacted between counterparties in the over-the-counter market, whereas futures are standardized contracts that are transacted on regulated exchanges.

Options are contractual agreements under which the seller (writer) grants the purchaser the right, but not the obligation, either to buy (call option) or sell (put option), by or at a set date, a specified amount of

a financial instrument at a predetermined price. The seller receives a premium from the purchaser for this right.

Credit derivatives are contracts whose redemption value is linked to specific credit related events, such as bankruptcy, credit downgrade, non-payment or default. Examples of credit derivatives include credit default swaps, total return swaps and credit default baskets.

Derivatives held or issued for trading purposes

Most of our derivative transactions relate to sales and trading activities. Sales activities include the structuring and marketing of derivative products to customers to enable them to transfer, modify or reduce current or expected risks. Trading involves market-making, positioning and arbitrage activities. Market-making involves quoting bid and offer prices to other market participants with the intention of generating revenues based on spread and volume. Positioning involves managing market risk positions with the expectation of profiting from favourable movements in prices, rates or indices. Arbitrage activities involve identifying and profiting from price differentials between markets and products. We do not deal, to any significant extent, in leveraged derivative transactions. These transactions contain a multiplier which, for any given change in market prices, could cause the change in the transaction's fair value to be significantly different from the change in fair value that would occur for a similar derivative without the multiplier.

Derivatives held or issued for non-trading purposes

We also use derivatives in connection with our own asset/liability management activities, which include hedging and investment activities.

Interest rate swaps are used to adjust exposure to interest rate risk by modifying the repricing or maturity characteristics of existing and/or anticipated assets and liabilities. As at October 31, 2002, the level of interest rate derivatives in place to hedge anticipated transactions, and accounted for as a hedge, was insignificant. Purchased interest rate options are used to hedge redeemable deposits and other options embedded in consumer products. Written options are used in our asset/liability management activities when specifically linked to a purchased

option in the form of a collar. We use credit derivatives to manage our credit exposures and for risk diversification in our lending portfolio. The amount of our deferred gains and losses associated with non-trading derivatives hedging anticipated transactions was insignificant.

Derivatives – Notional amounts

Notional amounts, which are off-balance sheet, serve as a point of reference for calculating payments and are a common measure of business volume. The following table provides the notional amounts of our derivative transactions by term to maturity.

Notional amount of derivatives by term to maturity

| | Term to maturity | | | | 2002 | | 2001 | |
|---|--------------------|-------------------|-------------------|--------------------|--------------------|--------------------|--------------------|--------------------|
| | Within 1 year | 1 to 5 years | Over 5 years (1) | Total | Trading | Other than trading | Trading | Other than trading |
| Over-the-counter (OTC) contracts | | | | | | | | |
| Interest rate contracts | | | | | | | | |
| Forward rate agreements | \$ 184,487 | \$ 14,358 | \$ – | \$ 198,845 | \$ 194,537 | \$ 4,308 | \$ 95,678 | \$ – |
| Swaps | 264,829 | 418,082 | 179,353 | 862,264 | 794,961 | 67,303 | 628,735 | 69,167 |
| Options purchased | 8,193 | 35,623 | 11,477 | 55,293 | 55,289 | 4 | 19,787 | 114 |
| Options written | 9,306 | 34,564 | 12,304 | 56,174 | 56,080 | 94 | 22,177 | – |
| Foreign exchange contracts | | | | | | | | |
| Forward contracts | 507,410 | 33,673 | 3,636 | 544,719 | 522,035 | 22,684 | 528,467 | 17,969 |
| Cross currency swaps | 893 | 3,405 | 5,609 | 9,907 | 9,907 | – | 8,618 | – |
| Cross currency interest rate swaps | 10,286 | 37,315 | 26,547 | 74,148 | 71,050 | 3,098 | 63,405 | 2,796 |
| Options purchased | 53,200 | 3,004 | – | 56,204 | 56,160 | 44 | 48,542 | 612 |
| Options written | 58,594 | 3,242 | – | 61,836 | 61,209 | 627 | 54,133 | – |
| Credit derivatives (2) | 3,625 | 37,333 | 11,193 | 52,151 | 50,928 | 1,223 | 20,952 | 955 |
| Other contracts (3) | 9,514 | 5,221 | 7,884 | 22,619 | 22,085 | 534 | 20,170 | 2,643 |
| Exchange-traded contracts | | | | | | | | |
| Interest rate contracts | | | | | | | | |
| Futures – long positions | 19,207 | 7,535 | 19 | 26,761 | 26,761 | – | 20,319 | – |
| Futures – short positions | 31,583 | 5,185 | 25 | 36,793 | 36,500 | 293 | 43,232 | 87 |
| Options purchased | 1,418 | 1 | – | 1,419 | 640 | 779 | 13,352 | – |
| Options written | 2,368 | 2 | – | 2,370 | 2,059 | 311 | 12,079 | – |
| Foreign exchange contracts | | | | | | | | |
| Futures – long positions | 27 | – | – | 27 | 27 | – | 348 | – |
| Futures – short positions | 321 | – | – | 321 | 321 | – | 144 | – |
| Other contracts (3) | 18,356 | 455 | – | 18,811 | 18,811 | – | 58,130 | – |
| | \$1,183,617 | \$ 638,998 | \$ 258,047 | \$2,080,662 | \$1,979,360 | \$ 101,302 | \$1,658,268 | \$ 94,343 |

(1) Includes contracts maturing in over 10 years with a notional value of \$37,322 million (2001 – \$19,637 million). The related gross positive replacement cost is \$1,291 million (2001 – \$950 million).

(2) Comprises credit default swaps, total return swaps and credit default baskets.

(3) Comprises precious metals, commodity and equity-linked derivative contracts.

Derivative-related credit risk

Credit risk from derivative transactions is generated by the potential for the counterparty to default on its contractual obligations when one or more transactions have a positive market value to us. This market value is referred to as replacement cost since it is an estimate of what it would cost to replace transactions at prevailing market rates if a default occurred.

For internal risk management purposes, the credit equivalent amount arising from a derivative transaction is defined as the sum of the replacement cost plus an add-on that is an estimate of the potential change in the market value of the transaction through to maturity. The add-on is determined by statistically based models that project the expected volatility of the variable(s) underlying the derivative, whether interest rate, foreign exchange rate, equity or commodity price. Both the replacement cost and the add-on are continually re-evaluated over the life of each transaction to ensure that sound credit risk valuations are used. The risk-adjusted amount is determined by applying standard measures of counterparty risk to the credit equivalent amount.

Netting is a technique that can reduce credit exposure from derivatives and is generally facilitated through the use of master netting agreements. The two main categories of netting are close-out netting and settlement netting. Under the close-out netting provision, if the counterparty defaults, we have the right to terminate all transactions covered by the master agreement at the then-prevailing market values and to sum the resulting market values, offsetting negative against positive values, to arrive at a single net amount owed either by us or the counterparty. Under the settlement netting provision, all payments and receipts in the same currency and due on the same day between specified pairs including us and the counterparty units are netted, generating a single

payment in each currency, due either by us or the counterparty unit. We actively encourage counterparties to enter into master netting agreements. However, measurement of our credit exposure arising out of derivative transactions is not reduced to reflect the effects of netting unless the enforceability of that netting is supported by appropriate legal analysis as documented in our policy.

To further manage derivative-related counterparty credit exposure, we enter into agreements containing mark-to-market cap provisions with some counterparties. Under such provisions, we have the right to request that the counterparty pay down or collateralize the current market value of its derivatives position with us. The use of collateral does not currently represent a significant credit mitigation technique for us in managing derivative-related credit risk.

We subject our derivative-related credit risks to the same credit approval, limit and monitoring standards that we use for managing other transactions that create credit exposure. This includes evaluation of counterparties as to creditworthiness, and managing the size, diversification and maturity structure of the portfolio. Credit utilization for all products is compared with established limits on a continual basis and is subject to a standard exception reporting process. We utilize a single internal rating system for all credit risk exposure. In most cases, these internal ratings approximate the external risk ratings of public rating agencies. The tables below show replacement cost, credit equivalent and risk-adjusted amounts of our derivatives both before and after the impact of netting. During 2002 and 2001, neither our actual credit losses arising from derivative transactions nor the level of impaired derivative contracts were significant.

NOTE 19 Derivative financial instruments (continued)**Replacement cost of derivative financial instruments by risk rating and by counterparty type**

| As at October 31, 2002 | Risk rating (1) | | | | | Counterparty type (2) | | | |
|--|-----------------|-----------|----------|-------------|-----------|-----------------------|------------------|----------|-----------|
| | AAA, AA | A | BBB | BB or lower | Total | Banks | OECD governments | Other | Total |
| Gross positive replacement cost (3) | \$ 15,442 | \$ 11,008 | \$ 3,421 | \$ 1,580 | \$ 31,451 | \$ 21,427 | \$ 2,068 | \$ 7,956 | \$ 31,451 |
| Impact of master netting agreements | (10,638) | (7,208) | (2,142) | (873) | (20,861) | (16,343) | – | (4,518) | (20,861) |
| Replacement cost (after netting agreements) | \$ 4,804 | \$ 3,800 | \$ 1,279 | \$ 707 | \$ 10,590 | \$ 5,084 | \$ 2,068 | \$ 3,438 | \$ 10,590 |
| Replacement cost (after netting agreements) – 2001 | \$ 3,583 | \$ 4,322 | \$ 1,515 | \$ 529 | \$ 9,949 | \$ 3,652 | \$ 1,892 | \$ 4,405 | \$ 9,949 |

- (1) Our internal risk ratings for major counterparty types approximate those of public rating agencies. Ratings of AAA, AA, A and BBB represent investment grade ratings and ratings of BB or lower represent non-investment grade ratings.
- (2) Counterparty type is defined in accordance with the capital adequacy requirements of the Superintendent of Financial Institutions Canada.
- (3) Represents the total current replacement value of all outstanding contracts in a gain position, before factoring in the impact of master netting agreements. Exchange-traded instruments are subject to daily margin requirements and are excluded as they are deemed to have no additional credit risk. The fair value of \$194 million (2001 – \$194 million) is excluded at October 31, 2002. Written options are excluded as they represent our obligations and as such do not attract credit risk.

Derivative-related credit risk

| | 2002 | | | 2001 | | |
|--|----------------------|------------------------------|---------------------------|----------------------|------------------------------|---------------------------|
| | Replacement cost (1) | Credit equivalent amount (2) | Risk-adjusted balance (3) | Replacement cost (1) | Credit equivalent amount (2) | Risk-adjusted balance (3) |
| Interest rate contracts | | | | | | |
| Forward rate agreements | \$ 178 | \$ 299 | \$ 64 | \$ 108 | \$ 543 | \$ 114 |
| Swaps | 19,608 | 24,357 | 6,323 | 17,568 | 21,390 | 5,617 |
| Options purchased | 563 | 914 | 258 | 416 | 538 | 123 |
| | 20,349 | 25,570 | 6,645 | 18,092 | 22,471 | 5,854 |
| Foreign exchange contracts | | | | | | |
| Forward contracts | 6,802 | 13,049 | 3,685 | 6,839 | 12,977 | 3,881 |
| Swaps | 1,781 | 6,341 | 1,445 | 1,902 | 5,536 | 1,261 |
| Options purchased | 809 | 1,491 | 439 | 721 | 1,339 | 441 |
| | 9,392 | 20,881 | 5,569 | 9,462 | 19,852 | 5,583 |
| Credit derivatives (4) | 861 | 2,963 | 858 | 87 | 1,249 | 369 |
| Other contracts (5) | 849 | 1,701 | 529 | 1,140 | 2,015 | 617 |
| Derivatives before master netting agreements | 31,451 | 51,115 | 13,601 | 28,781 | 45,587 | 12,423 |
| Impact of master netting agreements | (20,861) | (26,930) | (7,132) | (18,832) | (24,450) | (6,339) |
| Total derivatives after master netting agreements | \$ 10,590 | \$ 24,185 | \$ 6,469 | \$ 9,949 | \$ 21,137 | \$ 6,084 |

- (1) Represents the total current replacement value of all outstanding contracts in a gain position, before factoring in the impact of master netting agreements. Exchange-traded instruments are subject to daily margin requirements and are excluded as they are deemed to have no additional credit risk. The fair value of \$194 million (2001 – \$194 million) is excluded at October 31, 2002. Written options are excluded as they represent our obligations and as such do not attract credit risk.
- (2) Consists of (i) the total positive replacement value of all outstanding contracts, and (ii) an amount for potential future credit exposure.
- (3) Using guidelines issued by the Superintendent of Financial Institutions Canada.
- (4) Comprises credit default swaps, total return swaps and credit default baskets.
- (5) Comprises precious metals, commodity and equity-linked derivative contracts.

NOTE 20 Concentrations of credit risk

Concentrations of credit risk exist if a number of clients are engaged in similar activities, or are located in the same geographic region or have comparable economic characteristics such that their ability to meet contractual obligations would be similarly affected by changes in economic,

political or other conditions. Concentrations of credit risk indicate the relative sensitivity of our performance to developments affecting a particular industry or geographic location. The concentrations described below are within limits as established by management.

| 2002 | | | | | | | | | | 2001 | | | | | | | | | |
|---|-----------|-----|---------------|-----|-----------|-----|---------------------|----|-----------|-----------|-----|---------------|-----|-----------|-----|---------------------|----|-----------|--|
| | Canada | % | United States | % | Europe | % | Other International | % | Total | Canada | % | United States | % | Europe | % | Other International | % | Total | |
| On-balance sheet assets (1) | \$158,005 | 73% | \$ 32,442 | 15% | \$ 18,917 | 9% | \$ 5,979 | 3% | \$215,343 | \$164,371 | 76% | \$ 29,879 | 14% | \$ 16,724 | 8% | \$ 6,207 | 2% | \$217,181 | |
| Off-balance sheet credit instruments (2) | | | | | | | | | | | | | | | | | | | |
| Committed and uncommitted (3) | \$ 60,397 | 50% | \$ 45,573 | 38% | \$ 13,863 | 11% | \$ 1,191 | 1% | \$121,024 | \$ 76,832 | 56% | \$ 43,508 | 32% | \$ 14,465 | 10% | \$ 3,084 | 2% | \$137,889 | |
| Other | 23,266 | 61 | 10,723 | 28 | 4,235 | 11 | 148 | - | 38,372 | 20,990 | 59 | 9,893 | 28 | 4,436 | 12 | 331 | 1 | 35,650 | |
| | \$ 83,663 | 53% | \$ 56,296 | 35% | \$ 18,098 | 11% | \$ 1,339 | 1% | \$159,396 | \$ 97,822 | 56% | \$ 53,401 | 31% | \$ 18,901 | 11% | \$ 3,415 | 2% | \$173,539 | |
| Derivatives before master netting agreements (4), (5) | \$ 7,734 | 25% | \$ 9,887 | 31% | \$ 12,232 | 39% | \$ 1,598 | 5% | \$ 31,451 | \$ 6,899 | 24% | \$ 9,154 | 32% | \$ 11,741 | 41% | \$ 987 | 3% | \$ 28,781 | |

- (1) Includes assets purchased under reverse repurchase agreements, loans and customers' liability under acceptances. The largest concentrations in Canada are Ontario at 38% (2001 - 43%) and British Columbia at 11% (2001 - 11%). No industry accounts for more than 10% of total on-balance sheet credit instruments.
- (2) Represents financial instruments with contractual amounts representing credit risk.
- (3) Of the commitments to extend credit, the largest industry concentration relates to financial institutions at 35% (2001 - 34%), mining and energy at 15% (2001 - 15%), transportation at 8% (2001 - 10%) and manufacturing at 8% (2001 - 10%).
- (4) The largest concentration by counterparty type of this credit risk exposure is with banks at 68% (2001 - 64%).
- (5) Represents the total current replacement value of all outstanding contracts in a gain position, before factoring in the impact of master netting agreements. Exchange-traded instruments are subject to daily margin requirements and are excluded as they are deemed to have no additional credit risk. The fair value of \$194 million (2001 - \$194 million) is excluded at October 31, 2002. Written options are excluded as they represent our obligations and as such do not attract credit risk.

NOTE 21 Estimated fair value of financial instruments

The estimated fair values disclosed below are designed to approximate values at which these instruments could be exchanged in a current transaction between willing parties. However, many of the financial instruments lack an available trading market and therefore, fair values are based on estimates using net present value and other valuation techniques, which are significantly affected by the assumptions used concerning the amount and timing of estimated future cash flows and

discount rates, which reflect varying degrees of risk. Furthermore, due to the use of subjective judgment and uncertainties, the aggregate fair value amounts should not be interpreted as being realizable in an immediate settlement of the instruments.

The estimated fair values disclosed below do not reflect the value of assets and liabilities that are not considered financial instruments such as premises and equipment.

Financial assets and liabilities

| | 2002 | | | 2001 | | |
|--|------------|------------|------------|------------|------------|------------|
| | Book value | Fair value | Difference | Book value | Fair value | Difference |
| Financial assets | | | | | | |
| Cash resources | \$21,323 | \$21,323 | \$- | \$17,535 | \$17,535 | \$- |
| Securities | 93,800 | 94,251 | 451 | 80,507 | 80,937 | 430 |
| Assets purchased under reverse repurchase agreements | 35,831 | 35,831 | - | 35,870 | 35,870 | - |
| Loans | 169,258 | 171,546 | 2,288 | 169,110 | 173,263 | 4,153 |
| Customers' liability under acceptances | 8,051 | 8,051 | - | 9,923 | 9,923 | - |
| Other assets | 39,943 | 40,465 | 522 | 37,865 | 37,915 | 50 |
| Financial liabilities | | | | | | |
| Deposits | 243,486 | 245,136 | (1,650) | 233,447 | 236,196 | (2,749) |
| Acceptances | 8,051 | 8,051 | - | 9,923 | 9,923 | - |
| Obligations related to securities sold short | 19,110 | 19,110 | - | 16,443 | 16,443 | - |
| Obligations related to assets sold under repurchase agreements | 21,109 | 21,109 | - | 20,864 | 20,864 | - |
| Other liabilities | 57,760 | 57,760 | - | 51,918 | 51,198 | - |
| Subordinated debentures | 6,614 | 6,935 | (321) | 6,513 | 6,845 | (332) |

NOTE 21 Estimated fair value of financial instruments (continued)**Derivatives**

| | 2002 | | | | 2001 | |
|---|---|-----------|---------------------|-----------|---------------------|-----------|
| | Average fair value for the year ended (1) | | Year-end fair value | | Year-end fair value | |
| | Positive | Negative | Positive | Negative | Positive | Negative |
| Held or issued for trading purposes | | | | | | |
| Interest rate contracts | | | | | | |
| Forward rate agreements | \$ 96 | \$ 82 | \$ 178 | \$ 177 | \$ 108 | \$ 79 |
| Swaps | 13,650 | 14,323 | 18,468 | 18,930 | 16,211 | 16,692 |
| Options purchased | 385 | — | 564 | — | 442 | — |
| Options written | — | 325 | — | 474 | — | 352 |
| | 14,131 | 14,730 | 19,210 | 19,581 | 16,761 | 17,123 |
| Foreign exchange contracts | | | | | | |
| Forward contracts | 7,539 | 6,934 | 6,568 | 6,260 | 6,800 | 5,868 |
| Cross currency swaps | 501 | 294 | 504 | 340 | 518 | 315 |
| Cross currency interest rate swaps | 1,462 | 1,853 | 1,109 | 1,678 | 1,309 | 1,975 |
| Options purchased | 827 | — | 809 | — | 715 | — |
| Options written | — | 729 | — | 586 | — | 560 |
| | 10,329 | 9,810 | 8,990 | 8,864 | 9,342 | 8,718 |
| Credit derivatives (2) | 273 | 259 | 822 | 483 | 84 | 79 |
| Other contracts (3) | 1,077 | 2,853 | 1,028 | 3,093 | 1,012 | 2,650 |
| | \$ 25,810 | \$ 27,652 | 30,050 | 32,021 | 27,199 | 28,570 |
| Held or issued for other than trading purposes | | | | | | |
| Interest rate contracts | | | | | | |
| Forward rate agreements | | | — | 49 | — | — |
| Swaps | | | 1,140 | 842 | 1,357 | 1,104 |
| Options purchased | | | 1 | — | — | — |
| Options written | | | — | 13 | — | — |
| | | | 1,141 | 904 | 1,357 | 1,104 |
| Foreign exchange contracts | | | | | | |
| Forward contracts | | | 234 | 94 | 39 | 313 |
| Cross currency interest rate swaps | | | 168 | 24 | 75 | 50 |
| Options purchased | | | — | — | 6 | — |
| Options written | | | — | 3 | — | — |
| | | | 402 | 121 | 120 | 363 |
| Credit derivatives (2) | | | 39 | 8 | 3 | 3 |
| Other contracts (3) | | | 13 | — | 296 | 48 |
| | | | 1,595 | 1,033 | 1,776 | 1,518 |
| Total gross fair values before netting | | | 31,645 | 33,054 | 28,975 | 30,088 |
| Impact of master netting agreements | | | | | | |
| With intent to settle net or simultaneously (4) | | | (12) | (12) | (39) | (39) |
| Without intent to settle net or simultaneously (5) | | | (20,849) | (20,849) | (18,793) | (18,793) |
| Total | | | \$ 10,784 | \$ 12,193 | \$ 10,143 | \$ 11,256 |

(1) Average fair value amounts are calculated based on monthly balances.

(2) Comprises credit default swaps, total return swaps and credit default baskets.

(3) Comprises precious metals, commodity, equity-linked derivative contracts.

(4) Impact of offsetting credit exposures on contracts where we have both a legally enforceable master netting agreement in place and we intend to settle the contracts on either a net basis or simultaneously.

(5) Additional impact of offsetting credit exposures on contracts where we have a legally enforceable master netting agreement in place but do not intend to settle the contracts on a net basis or simultaneously.

Methodologies and assumptions used to estimate fair values of financial instruments

Loans The fair value of the business and government loans portfolio is based on an assessment of two key risks as appropriate; interest rate risk and credit risk. Fair value is determined under a discounted cash flow methodology using a discount rate based on interest rates currently charged for new loans with similar terms and remaining maturities, adjusted for a credit risk factor, which is reviewed at least annually. Fair value of the consumer loan portfolio is based on a discounted cash flow methodology adjusted principally for prepayment risk. For certain variable rate loans that reprice frequently and loans without a stated maturity, fair values are assumed to be equal to carrying values.

Securities The fair values of securities are provided in the Securities note to the consolidated financial statements (note 5). These are based on quoted market prices, when available. If quoted market prices are not available, fair values are estimated using quoted market prices of similar securities.

Deposits The fair values of fixed rate deposits with a fixed maturity are determined by discounting the expected future cash flows, using market interest rates currently offered for deposits of similar terms and remaining maturities (adjusted for early redemptions where appropriate). The fair values of deposits with no stated maturity or deposits with floating rates are assumed to be equal to their carrying values.

Other assets/liabilities The carrying values of Other assets and Other liabilities approximate their fair values with the exception of amounts relating to derivative financial instruments held or issued for other than trading purposes. The net fair value over book value for these instruments is shown in Other assets.

Subordinated debentures The fair values of subordinated debentures are based on quoted market prices for similar issues, or current rates offered to us for debt of the same remaining maturity.

Financial instruments valued at carrying value Due to their short term nature, the fair value of cash resources, assets purchased under reverse repurchase agreements, customers' liability under acceptances, our liability under acceptances, obligations related to securities sold short and obligations related to assets sold under repurchase agreements is assumed to approximate carrying value.

Derivative financial instruments The fair values of derivative financial instruments are determined using various methodologies. For exchange-traded instruments, fair value is based on quoted market prices, where available. For non-exchange-traded instruments or where no quoted market prices are available, fair value is based on prevailing market rates for instruments with similar characteristics and maturities, net present value analysis or other pricing models as appropriate.

NOTE 22 Contractual repricing and maturity schedule

The table below details our exposure to interest rate risk as defined and prescribed by the Canadian Institute of Chartered Accountants handbook Section 3860, *Financial Instruments – Disclosure and Presentation*. On- and off-balance sheet financial instruments are reported based on the earlier of their contractual repricing date or maturity date. Effective interest rates have been disclosed where applicable. The effective rates shown represent historical rates for fixed-rate instruments carried at amortized cost and current market rates for floating-rate instruments or instruments carried at fair value.

The table below does not incorporate management's expectation of future events where expected repricing or maturity dates differ significantly from the contractual dates. We incorporate these assumptions in the management of interest rate risk exposure. These assumptions include expected repricing of trading instruments and certain loans and deposits. Taking into account these assumptions on the consolidated contractual repricing and maturity schedule at October 31, 2002, would result in a change in the under-one-year gap from \$(37.5) billion to \$(3.7) billion (2001 – \$(35.3) billion to \$(19.1) billion).

Carrying amount by earlier of contractual repricing or maturity date

| | Immediately rate-sensitive | Under 3 months | 3 to 6 months | Over 6 to 12 months | Over 1 to 5 years | Over 5 years | Non-interest- sensitive | Total |
|---|-------------------------------|-------------------|------------------|------------------------|----------------------|-----------------|----------------------------|-----------|
| Assets | | | | | | | | |
| Cash resources | \$ – | \$ 16,483 | \$ 1,760 | \$ 2,013 | \$ 78 | \$ – | \$ 989 | \$ 21,323 |
| Effective interest rate | | 2.32% | 2.16% | 2.10% | 2.21% | | | |
| Securities | | | | | | | | |
| Trading account | – | 13,400 | 4,483 | 3,358 | 10,634 | 12,131 | 24,322 | 68,328 |
| Effective interest rate | | 2.31% | 2.07% | 2.96% | 3.79% | 4.73% | | |
| Investment account and loan substitute | – | 5,173 | 2,120 | 2,938 | 10,257 | 3,553 | 1,431 | 25,472 |
| Effective interest rate | | 3.41% | 3.00% | 3.37% | 3.88% | 4.81% | | |
| Assets purchased under reverse repurchase agreements | – | 34,990 | 300 | 515 | 1 | 2 | 23 | 35,831 |
| Effective interest rate | | 2.54% | 2.86% | 3.05% | 2.94% | 3.88% | | |
| Loans | 44,116 | 41,621 | 8,223 | 11,518 | 57,949 | 5,746 | 85 | 169,258 |
| Effective interest rate | | 3.51% | 4.74% | 5.66% | 6.03% | 6.19% | | |
| Other assets | – | – | – | – | – | – | 56,744 | 56,744 |
| | 44,116 | 111,667 | 16,886 | 20,342 | 78,919 | 21,432 | 83,594 | 376,956 |
| Liabilities | | | | | | | | |
| Deposits | 98,018 | 79,301 | 13,420 | 22,279 | 28,397 | 2,071 | – | 243,486 |
| Effective interest rate | | 1.80% | 2.28% | 2.80% | 4.06% | 4.11% | | |
| Obligations related to securities sold short | – | 1,581 | 236 | 465 | 5,858 | 5,285 | 5,685 | 19,110 |
| Effective interest rate | | 3.81% | 2.77% | 2.84% | 3.71% | 5.16% | | |
| Obligations related to assets sold under repurchase agreements | – | 19,874 | 516 | 667 | – | – | 52 | 21,109 |
| Effective interest rate | | 2.54% | 2.91% | 3.05% | | | | |
| Other liabilities | – | – | – | – | – | – | 66,385 | 66,385 |
| Subordinated debentures | – | 1,348 | – | 100 | 3,263 | 1,903 | – | 6,614 |
| Effective interest rate | | 2.40% | | 5.45% | 6.25% | 7.04% | | |
| Non-controlling interest in subsidiaries | – | – | – | – | – | 1,400 | 69 | 1,469 |
| Effective interest rate | | | | | | 7.23% | | |
| Shareholders' equity | – | – | – | – | 700 | 845 | 17,238 | 18,783 |
| Effective interest rate | | | | | 6.40% | 5.63% | | |
| | 98,018 | 102,104 | 14,172 | 23,511 | 38,218 | 11,504 | 89,429 | 376,956 |
| On-balance sheet gap | (53,902) | 9,563 | 2,714 | (3,169) | 40,701 | 9,928 | (5,835) | – |
| Off-balance sheet financial instruments (1) | | | | | | | | |
| Derivatives used for asset liability management purposes | | | | | | | | |
| Pay side instruments | – | (36,659) | (734) | (2,442) | (23,421) | (4,655) | – | (67,911) |
| Effective interest rate | | 5.20% | 5.32% | 4.52% | 5.14% | 5.70% | | |
| Receive side instruments | – | 34,758 | 1,958 | 6,235 | 19,085 | 5,875 | – | 67,911 |
| Effective interest rate | | 5.01% | 3.61% | 3.61% | 5.34% | 6.08% | | |
| Derivatives used for trading purposes | – | 2,223 | (59) | 2,033 | (383) | 2,731 | (6,545) | – |
| Effective interest rate | | 2.82% | 2.88% | 2.98% | 3.69% | 5.04% | | |
| | – | 322 | 1,165 | 5,826 | (4,719) | 3,951 | (6,545) | – |
| Total gap | \$ (53,902) | \$ 9,885 | \$ 3,879 | \$ 2,657 | \$ 35,982 | \$ 13,879 | \$ (12,380) | \$ – |
| Canadian dollar | (28,828) | 9,104 | 3,614 | 112 | 30,953 | 4,475 | (19,896) | (466) |
| Foreign currency | (25,074) | 781 | 265 | 2,545 | 5,029 | 9,404 | 7,516 | 466 |
| Total gap | \$ (53,902) | \$ 9,885 | \$ 3,879 | \$ 2,657 | \$ 35,982 | \$ 13,879 | \$ (12,380) | \$ – |
| Canadian dollar – 2001 | (8,064) | (786) | (7,292) | (4,784) | 38,156 | 1,759 | (24,598) | (5,609) |
| Foreign currency – 2001 | (18,137) | 8,390 | (4,529) | (136) | 4,540 | 5,924 | 9,557 | 5,609 |
| Total gap – 2001 | \$ (26,201) | \$ 7,604 | \$ (11,821) | \$ (4,920) | \$ 42,696 | \$ 7,683 | \$ (15,041) | \$ – |

(1) Represents net notional amounts.

NOTE 23

Reconciliation of Canadian and United States generally accepted accounting principles

These consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles (GAAP), including the accounting requirements of the Superintendent of Financial

Institutions Canada. As required by the United States Securities and Exchange Commission, material differences between Canadian and United States GAAP are described below.

Summary of reconciliation to U.S. GAAP

| | 2002 | | | 2001 | | | 2000 | | |
|---|-----------------|----------------------|-------------------|-----------------|----------------------|-------------------|-----------------|----------------------|-------------------|
| | Net income | Shareholders' equity | Assets | Net income | Shareholders' equity | Assets | Net income | Shareholders' equity | Assets |
| Canadian GAAP | \$ 2,762 | \$ 18,783 | \$ 376,956 | \$ 2,411 | \$ 18,165 | \$ 359,260 | \$ 2,274 | \$ 13,541 | \$ 289,740 |
| Insurance accounting (1) | 72 | 92 | 1,969 | 41 | 19 | 1,290 | (29) | (13) | 416 |
| Derivative instruments and hedging activities (2) | 56 | (72) | 925 | (1) | (191) | 1,235 | — | — | — |
| Costs of Stock Appreciation Rights (3) | 10 | 7 | (4) | — | — | — | — | — | — |
| Additional pension obligation (4) | — | (293) | 167 | — | (17) | 12 | — | — | — |
| Reclassification of securities (5) | — | 210 | 210 | — | 199 | 199 | — | (56) | (46) |
| Trade date accounting (6) | — | — | (146) | — | — | (1,464) | — | — | 419 |
| Substantively enacted tax rate change (7) | — | — | — | (16) | — | — | 16 | 16 | 16 |
| Postretirement benefits other than pensions (8) | — | — | — | — | — | — | (35) | (163) | 123 |
| Pension benefits (8) | — | — | — | — | — | — | — | (27) | (27) |
| Other (9) | (2) | 28 | 1,855 | — | 30 | 1,951 | (18) | (1) | 3,413 |
| U.S. GAAP | \$ 2,898 | \$ 18,755 | \$ 381,932 | \$ 2,435 | \$ 18,205 | \$ 362,483 | \$ 2,208 | \$ 13,297 | \$ 294,054 |
| Earnings per share | \$ 4.16 | | | \$ 3.58 | | | \$ 3.42 | | |
| Diluted earnings per share | \$ 4.12 | | | \$ 3.55 | | | \$ 3.40 | | |

- (1) There are differences between U.S. and Canadian GAAP treatment with respect to life insurance premiums, investment accounting, acquisition costs and claims and policy benefit liabilities. These lead to timing differences in income and expense recognition. The application of U.S. GAAP to our insurance operations would increase Net income by \$72 million for the year ended October 31, 2002. Differences with respect to deferred acquisition costs and claims and policy benefit liabilities would account for \$24 million and \$32 million of the increase, respectively. The increase would also include \$16 million of realized gains on investments, which are taken into income as realized under U.S. GAAP but deferred and amortized under Canadian GAAP. Other assets and Other liabilities would increase by \$1,969 million and \$1,877 million, respectively and Shareholders' equity would increase by \$92 million as at October 31, 2002.
- (2) Under U.S. GAAP, all derivatives are recorded on the balance sheet at fair value. Changes in the fair value of derivatives are recorded in Net income, or if the derivative is designated and to the extent it functions effectively as a cash flow hedge, in Other comprehensive income within Shareholders' equity. For derivatives designated as fair value hedges, the changes recorded in Net income are generally offset by changes in the fair value of the hedged item attributable to the risk being hedged. The changes recorded in Other comprehensive income are subsequently amortized to Net income to offset the effects of interest rate variability on cash flows of the hedged item. Under Canadian GAAP, derivatives used in sales and trading activities are recorded on the balance sheet at fair value with changes in fair value recorded in Net income. Recording derivatives and hedging activities in accordance with U.S. GAAP would increase Net income by \$56 million for the year ended October 31, 2002, increase Securities by \$82 million, Loans by \$62 million, Other assets by \$811 million, Deposits by \$175 million, Other liabilities by \$476 million and Subordinated debentures by \$346 million, and decrease Cash resources by \$30 million, and Shareholders' equity by \$72 million as at October 31, 2002.
- (3) Between November 29, 1999 and June 5, 2001, grants of options under the employee stock option plan were accompanied by tandem stock appreciation rights (SARs). With SARs, participants could choose to exercise a SAR instead of the corresponding option. In such cases, the participants received a cash payment equal to the difference between the closing price of common shares on the day immediately preceding the day of exercise and the exercise price of the option. For such plans, compensation expense under U.S. GAAP would be measured using estimates based on past experience of participants exercising SARs rather than the corresponding options. However, Canadian GAAP considers such a plan to result in a liability and requires measurement of compensation expense assuming that all participants will exercise SARs. Recognizing compensation expense in accordance with U.S. GAAP would increase Net income by \$10 million for the year ended October 31, 2002 and reduce Other liabilities by \$11 million as at October 31, 2002. The related income tax effects would reduce Other assets by \$4 million and Shareholders' equity would increase by \$7 million as at October 31, 2002.
- (4) For defined benefit pension plans, U.S. GAAP requires that the excess of the unfunded accumulated benefit obligation over the unrecognized prior service cost be recorded in Other comprehensive income. Recognition of this additional pension obligation would increase Other liabilities by \$460 million, the related deferred income taxes would increase Other assets by \$167 million and Shareholders' equity would decrease by \$293 million as at October 31, 2002.

- (5) Under U.S. GAAP, Securities are classified as Trading account (carried at estimated fair value) or Available for sale (carried at estimated fair value). The net unrealized gain (loss) on Available for sale securities, net of related income taxes, is reported as Other comprehensive income within Shareholders' equity except where the changes in market value are effectively hedged by derivatives. These hedged unrealized gains (losses) are recorded in Net income, where they are generally offset by the changes in fair value of the hedging derivatives. Under Canadian GAAP, Securities are classified as Investment account (carried at amortized cost) or Trading account (carried at estimated fair value). Classifying Securities in accordance with U.S. GAAP would increase Securities by \$342 million, decrease the related deferred income taxes included in Other assets by \$132 million, and increase Shareholders' equity by \$210 million as at October 31, 2002.
- (6) Under U.S. GAAP, trade date accounting for Securities is used for both the Consolidated balance sheet and the consolidated statement of income. Our practice under Canadian GAAP is settlement date accounting for the Consolidated balance sheet and trade date accounting for the consolidated statement of income. The application of trade date accounting to our Consolidated balance sheet would decrease Securities by \$220 million and Other liabilities by \$146 million, and increase Other assets by \$74 million as at October 31, 2002.
- (7) Under U.S. GAAP, the effects of changes in tax rates on deferred income taxes are recorded when the tax rate change has been passed into law. Under Canadian GAAP, these effects are recorded when the tax rate change has been substantively enacted. The reductions in the corporate tax rate announced during calendar year 2000 and considered substantively enacted then, were passed into law in 2001.
- (8) We adopted the new accounting standard issued by the CICA for *Employee Future Benefits* which requires us to accrue the costs of all postretirement benefits over the working lives of employees instead of the previous method of expensing costs when paid. The new standard also requires a change to the discount rate used to value future benefit obligations from an estimated long-term rate to a market-based interest rate. As a result of adopting this new standard on November 1, 2000, there are no longer differences between Canadian and U.S. GAAP related to employee future benefits accounting except as noted in footnote (4).
- (9) Other differences between U.S. and Canadian GAAP relate to the right of offset, accounting for joint ventures and other minor items. Investments in joint ventures are proportionately consolidated under Canadian GAAP and accounted for under the equity method under U.S. GAAP. Accounting for joint ventures in accordance with U.S. GAAP would not affect Net income. The net of these items would reduce Net income by \$2 million for the year ended October 31, 2002, increase Shareholders' equity by \$28 million, Assets by \$1,855 million and Liabilities by \$1,827 million as at October 31, 2002.

Supplementary information

Consolidated balance sheet

| As at October 31 (\$ millions) | 2002 | 2001 | 2000 | 1999 | 1998 | 1997 | 1996 | 1995 | 1994 | 1993 | 1992 |
|---|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|
| Assets | | | | | | | | | | | |
| Cash resources | \$ 21,323 | \$ 17,535 | \$ 16,408 | \$ 23,042 | \$ 16,395 | \$ 21,392 | \$ 23,567 | \$ 17,710 | \$ 16,449 | \$ 10,874 | \$ 10,938 |
| Securities | 93,800 | 80,507 | 60,208 | 50,559 | 41,399 | 33,037 | 43,490 | 32,705 | 27,695 | 24,011 | 16,146 |
| Reverse repurchase agreements | 35,831 | 35,870 | 18,303 | 20,272 | 19,907 | 18,642 | 11,446 | 4,591 | 5,259 | 5,304 | 607 |
| Loans | | | | | | | | | | | |
| Residential mortgage | 72,840 | 67,442 | 62,984 | 59,242 | 57,069 | 53,369 | 48,120 | 45,131 | 44,109 | 43,781 | 32,609 |
| Personal | 31,956 | 32,511 | 28,019 | 25,255 | 22,761 | 20,864 | 18,440 | 16,923 | 16,508 | 16,487 | 15,462 |
| Credit card | 4,914 | 4,283 | 4,666 | 2,666 | 1,945 | 2,324 | 3,522 | 3,435 | 3,321 | 3,090 | 2,532 |
| Business and government | 61,751 | 67,152 | 60,546 | 57,676 | 65,598 | 62,837 | 56,138 | 51,500 | 48,748 | 52,062 | 52,502 |
| | 171,461 | 171,388 | 156,215 | 144,839 | 147,373 | 139,394 | 126,220 | 116,989 | 112,686 | 115,420 | 103,105 |
| Allowance for loan losses | (2,203) | (2,278) | (1,871) | (1,884) | (2,026) | (1,769) | (1,875) | (2,003) | (2,559) | (4,255) | (3,575) |
| | 169,258 | 169,110 | 154,344 | 142,955 | 145,347 | 137,625 | 124,345 | 114,986 | 110,127 | 111,165 | 99,530 |
| Other | | | | | | | | | | | |
| Customers' liability under acceptances | 8,051 | 9,923 | 11,628 | 9,257 | 10,620 | 10,561 | 7,423 | 6,300 | 6,205 | 6,302 | 5,737 |
| Derivative-related amounts (1) | 30,258 | 27,240 | 19,155 | 15,151 | 30,413 | 14,776 | 12,994 | 12,378 | - | - | - |
| Premises and equipment | 1,653 | 1,602 | 1,249 | 1,320 | 1,872 | 1,696 | 1,785 | 1,870 | 1,975 | 2,057 | 1,914 |
| Goodwill | 5,004 | 4,919 | 648 | 611 | 551 | 607 | 335 | 333 | 365 | 447 | 195 |
| Other intangibles | 665 | 619 | 208 | - | - | - | - | - | - | - | - |
| Other assets | 11,113 | 11,935 | 7,589 | 7,483 | 7,895 | 6,438 | 6,113 | 5,157 | 5,004 | 4,781 | 3,226 |
| | 56,744 | 56,238 | 40,477 | 33,822 | 51,351 | 34,078 | 28,650 | 26,038 | 13,549 | 13,587 | 11,072 |
| | \$ 376,956 | \$ 359,260 | \$ 289,740 | \$ 270,650 | \$ 274,399 | \$ 244,774 | \$ 231,498 | \$ 196,030 | \$ 173,079 | \$ 164,941 | \$ 138,293 |
| Liabilities and shareholders' equity | | | | | | | | | | | |
| Deposits | | | | | | | | | | | |
| Personal | \$ 101,892 | \$ 101,381 | \$ 89,632 | \$ 87,359 | \$ 85,910 | \$ 86,106 | \$ 90,774 | \$ 89,929 | \$ 85,214 | \$ 84,696 | \$ 67,648 |
| Business and government | 119,591 | 107,141 | 93,618 | 86,223 | 76,107 | 64,368 | 47,799 | 39,900 | 36,422 | 33,781 | 30,245 |
| Bank | 22,003 | 24,925 | 19,646 | 14,315 | 17,988 | 22,755 | 23,244 | 13,662 | 14,179 | 11,922 | 14,329 |
| | 243,486 | 233,447 | 202,896 | 187,897 | 180,005 | 173,229 | 161,817 | 143,491 | 135,815 | 130,399 | 112,222 |
| Other | | | | | | | | | | | |
| Acceptances | 8,051 | 9,923 | 11,628 | 9,257 | 10,620 | 10,561 | 7,423 | 6,300 | 6,205 | 6,302 | 5,737 |
| Securities sold short | 19,110 | 16,443 | 13,419 | 17,885 | 14,404 | 11,152 | 8,331 | 7,128 | 5,569 | 5,362 | 3,628 |
| Repurchase agreements | 21,109 | 20,864 | 9,005 | 9,396 | 11,264 | 9,458 | 16,526 | 4,090 | 5,341 | 2,533 | 787 |
| Derivative-related amounts (1) | 32,137 | 28,646 | 18,574 | 15,219 | 29,370 | 14,732 | 13,449 | 12,384 | - | - | - |
| Other liabilities | 26,197 | 23,780 | 14,149 | 13,682 | 12,258 | 10,494 | 10,828 | 9,970 | 7,986 | 8,919 | 5,232 |
| | 106,604 | 99,656 | 66,775 | 65,439 | 77,916 | 56,397 | 56,557 | 39,872 | 25,101 | 23,116 | 15,384 |
| Subordinated debentures | 6,614 | 6,513 | 5,825 | 4,596 | 4,087 | 4,227 | 3,602 | 3,528 | 3,481 | 3,410 | 3,106 |
| Non-controlling interest in subsidiaries | 1,469 | 1,479 | 703 | 103 | 499 | 531 | 108 | 107 | 93 | 86 | 75 |
| Shareholders' equity | | | | | | | | | | | |
| Capital stock | | | | | | | | | | | |
| Preferred | 1,545 | 2,024 | 2,037 | 2,009 | 2,144 | 1,784 | 1,752 | 1,990 | 2,266 | 2,248 | 1,594 |
| Common | 7,057 | 6,973 | 3,076 | 3,065 | 2,925 | 2,907 | 2,876 | 2,910 | 2,910 | 2,910 | 2,910 |
| Retained earnings | 10,181 | 9,168 | 8,428 | 7,541 | 6,823 | 5,699 | 4,786 | 4,132 | 3,413 | 2,772 | 3,002 |
| | 18,783 | 18,165 | 13,541 | 12,615 | 11,892 | 10,390 | 9,414 | 9,032 | 8,589 | 7,930 | 7,506 |
| | \$ 376,956 | \$ 359,260 | \$ 289,740 | \$ 270,650 | \$ 274,399 | \$ 244,774 | \$ 231,498 | \$ 196,030 | \$ 173,079 | \$ 164,941 | \$ 138,293 |

(1) As the information is not reasonably determinable, amounts for years prior to 1995 have not been restated to reflect the presentation of derivative-related amounts on a gross basis.

Consolidated statement of income

| For the year ended October 31 (\$ millions, except per share amounts) | 2002 | 2001 | 2000 | 1999 | 1998 | 1997 | 1996 | 1995 | 1994 | 1993 | 1992 |
|--|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|---------------|----------------|
| Interest income | | | | | | | | | | | |
| Loans | \$ 10,463 | \$ 12,032 | \$ 11,538 | \$ 10,394 | \$ 10,474 | \$ 9,354 | \$ 9,490 | \$ 9,820 | \$ 8,693 | \$ 8,156 | \$ 8,957 |
| Securities | 3,075 | 3,281 | 2,669 | 2,190 | 1,914 | 2,166 | 2,461 | 2,179 | 1,654 | 1,320 | 1,037 |
| Assets purchased under reverse repurchase agreements (1) | 651 | 1,163 | 1,078 | 893 | 1,169 | 568 | 366 | 237 | 206 | 91 | — |
| Deposits with banks | 483 | 831 | 824 | 726 | 750 | 983 | 891 | 792 | 454 | 296 | 396 |
| | 14,672 | 17,307 | 16,109 | 14,203 | 14,307 | 13,071 | 13,208 | 13,028 | 11,007 | 9,863 | 10,390 |
| Interest expense | | | | | | | | | | | |
| Deposits | 5,709 | 8,712 | 9,057 | 7,636 | 7,732 | 6,548 | 7,115 | 7,362 | 5,477 | 4,995 | 5,868 |
| Other liabilities | 1,399 | 1,668 | 1,429 | 1,161 | 1,172 | 1,139 | 1,126 | 792 | 761 | 567 | 322 |
| Subordinated debentures | 406 | 410 | 344 | 286 | 339 | 384 | 322 | 335 | 290 | 263 | 272 |
| | 7,514 | 10,790 | 10,830 | 9,083 | 9,243 | 8,071 | 8,563 | 8,489 | 6,528 | 5,825 | 6,462 |
| Net interest income | 7,158 | 6,517 | 5,279 | 5,120 | 5,064 | 5,000 | 4,645 | 4,539 | 4,479 | 4,038 | 3,928 |
| Provision for credit losses | 1,065 | 1,119 | 691 | 760 | 575 | 380 | 440 | 580 | 820 | 1,750 | 2,050 |
| | 6,093 | 5,398 | 4,588 | 4,360 | 4,489 | 4,620 | 4,205 | 3,959 | 3,659 | 2,288 | 1,878 |
| Other income | | | | | | | | | | | |
| Capital market fees | 1,866 | 1,523 | 1,538 | 1,028 | 918 | 1,172 | 764 | 434 | 567 | 456 | 356 |
| Trading revenues | 1,766 | 1,820 | 1,540 | 1,106 | 748 | 606 | 368 | 362 | 345 | 414 | 387 |
| Investment management and custodial fees | 1,179 | 1,096 | 860 | 651 | 605 | 404 | 319 | 286 | 278 | 101 | 82 |
| Deposit and payment service charges | 1,041 | 887 | 756 | 688 | 664 | 690 | 701 | 681 | 661 | 649 | 654 |
| Mutual fund revenues | 723 | 692 | 624 | 556 | 537 | 354 | 241 | 190 | 202 | 64 | 37 |
| Card service revenues | 496 | 458 | 420 | 362 | 305 | 332 | 282 | 278 | 258 | 203 | 183 |
| Foreign exchange revenues, other than trading | 279 | 312 | 299 | 243 | 218 | 211 | 165 | 140 | 134 | 107 | 115 |
| Credit fees | 223 | 237 | 212 | 189 | 183 | 169 | 153 | 156 | 156 | 152 | 152 |
| Mortgage banking revenues | 222 | 206 | — | — | — | — | — | — | — | — | — |
| Insurance revenues | 204 | 201 | 191 | 161 | 113 | 102 | 70 | 104 | 100 | 61 | 32 |
| Securitization revenues | 174 | 123 | 115 | 222 | 218 | — | — | — | — | — | — |
| Gain (loss) on sale of securities | (116) | (128) | (11) | 28 | 343 | 37 | 107 | 17 | 49 | 169 | 14 |
| Gain from divestitures | — | 445 | — | — | — | — | — | — | — | — | — |
| Other | 505 | 343 | 188 | 246 | 133 | 202 | 96 | 90 | 113 | 75 | 90 |
| | 8,562 | 8,215 | 6,732 | 5,480 | 4,985 | 4,279 | 3,266 | 2,738 | 2,863 | 2,451 | 2,102 |
| Non-interest expense | | | | | | | | | | | |
| Human resources | 6,315 | 5,723 | 4,651 | 4,013 | 3,594 | 3,365 | 2,851 | 2,563 | 2,675 | 2,386 | 2,170 |
| Occupancy | 796 | 724 | 570 | 564 | 508 | 559 | 507 | 473 | 500 | 593 | 476 |
| Equipment | 820 | 771 | 665 | 677 | 585 | 605 | 492 | 506 | 460 | 473 | 382 |
| Communications | 801 | 686 | 695 | 699 | 665 | 587 | 523 | 461 | 450 | 377 | 372 |
| Professional fees | 419 | 412 | 267 | 298 | 262 | 228 | 165 | 147 | 113 | 86 | 88 |
| Amortization of goodwill | — | 248 | 76 | 66 | 62 | 59 | 38 | 38 | 48 | 35 | 19 |
| Amortization of other intangibles | 72 | 36 | 11 | — | — | — | — | — | — | — | — |
| Other | 1,197 | 1,155 | 646 | 743 | 723 | 650 | 536 | 469 | 415 | 465 | 410 |
| | 10,420 | 9,755 | 7,581 | 7,060 | 6,399 | 6,053 | 5,112 | 4,657 | 4,661 | 4,415 | 3,917 |
| Net income before income taxes | 4,235 | 3,858 | 3,739 | 2,780 | 3,075 | 2,846 | 2,359 | 2,040 | 1,861 | 324 | 63 |
| Income taxes | 1,365 | 1,340 | 1,445 | 1,015 | 1,175 | 1,090 | 880 | 755 | 655 | (5) | (65) |
| Net income before, non-controlling interest | 2,870 | 2,518 | 2,294 | 1,765 | 1,900 | 1,756 | 1,479 | 1,285 | 1,206 | 329 | 128 |
| Non-controlling interest | 108 | 107 | 20 | 8 | 76 | 77 | 49 | 23 | 37 | 29 | 21 |
| Net income | \$ 2,762 | \$ 2,411 | \$ 2,274 | \$ 1,757 | \$ 1,824 | \$ 1,679 | \$ 1,430 | \$ 1,262 | \$ 1,169 | \$ 300 | \$ 107 |
| Preferred share dividends | 98 | 135 | 134 | 157 | 145 | 131 | 144 | 164 | 168 | 154 | 123 |
| Net income available to common shareholders | \$ 2,664 | \$ 2,276 | \$ 2,140 | \$ 1,600 | \$ 1,679 | \$ 1,548 | \$ 1,286 | \$ 1,098 | \$ 1,001 | \$ 146 | \$ (16) |
| Earnings per share (loss) | | | | | | | | | | | |
| Basic | \$ 3.96 | \$ 3.55 | \$ 3.53 | \$ 2.55 | \$ 2.72 | \$ 2.50 | \$ 2.05 | \$ 1.75 | \$ 1.60 | \$ 0.23 | \$ (0.03) |
| Diluted | 3.93 | 3.52 | 3.51 | 2.53 | 2.67 | 2.46 | 2.05 | 1.75 | 1.60 | 0.23 | (0.03) |

(1) Amounts for assets purchased under reverse repurchase agreements are included in loans for 1992.

Consolidated statement of changes in shareholders' equity

| For the year ended October 31 (\$ millions) | 2002 | 2001 | 2000 | 1999 | 1998 | 1997 | 1996 | 1995 | 1994 | 1993 | 1992 |
|--|------------------|------------------|------------------|------------------|------------------|------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Preferred shares | | | | | | | | | | | |
| Balance at beginning of year | \$ 2,024 | \$ 2,037 | \$ 2,009 | \$ 2,144 | \$ 1,784 | \$ 1,752 | \$ 1,990 | \$ 2,266 | \$ 2,248 | \$ 1,594 | \$ 1,661 |
| Issued | — | 250 | — | 296 | 300 | — | — | — | — | 612 | — |
| Redeemed for cancellation | (468) | (300) | — | (400) | — | — | (237) | (272) | — | — | (102) |
| Translation adjustment | (11) | 37 | 28 | (31) | 60 | 32 | (1) | (4) | 18 | 42 | 35 |
| Balance at end of year | 1,545 | 2,024 | 2,037 | 2,009 | 2,144 | 1,784 | 1,752 | 1,990 | 2,266 | 2,248 | 1,594 |
| Common shares | | | | | | | | | | | |
| Balance at beginning of year | 6,973 | 3,076 | 3,065 | 2,925 | 2,907 | 2,876 | 2,910 | 2,910 | 2,910 | 2,910 | 2,726 |
| Issued | 236 | 4,009 | 109 | 192 | 18 | 69 | — | — | — | — | 184 |
| Purchased for cancellation | (152) | (112) | (98) | (52) | — | (38) | (34) | — | — | — | — |
| Balance at end of year | 7,057 | 6,973 | 3,076 | 3,065 | 2,925 | 2,907 | 2,876 | 2,910 | 2,910 | 2,910 | 2,910 |
| Retained earnings | | | | | | | | | | | |
| Balance at beginning of year (1) | 9,168 | 8,428 | 7,541 | 6,823 | 5,699 | 4,786 | 4,057 | 3,413 | 2,772 | 3,002 | 3,375 |
| Net income | 2,762 | 2,411 | 2,274 | 1,757 | 1,824 | 1,679 | 1,430 | 1,262 | 1,169 | 300 | 107 |
| Dividends – preferred | (98) | (135) | (134) | (157) | (145) | (131) | (144) | (164) | (168) | (154) | (123) |
| Dividends – common | (1,022) | (897) | (689) | (588) | (543) | (469) | (418) | (371) | (364) | (364) | (361) |
| Cumulative effect of initial adoption of <i>Employee Future Benefits</i> accounting standard (2) | — | (221) | — | — | — | — | — | — | — | — | — |
| Premium paid on common shares purchased | (612) | (397) | (562) | (281) | — | (160) | (136) | — | — | — | — |
| Issuance costs (2) | (1) | (19) | (4) | (9) | (7) | — | — | — | — | (11) | — |
| Change in unrealized foreign currency translation gains and losses | (59) | 473 | (2) | (205) | 164 | 129 | (12) | (23) | 96 | (4) | 16 |
| Impact of hedging unrealized foreign currency translation gains and losses (2) | 43 | (475) | 4 | 201 | (169) | (135) | 9 | 15 | (92) | 3 | (12) |
| Balance at end of year | 10,181 | 9,168 | 8,428 | 7,541 | 6,823 | 5,699 | 4,786 | 4,132 | 3,413 | 2,772 | 3,002 |
| Shareholders' equity at end of year | \$ 18,783 | \$ 18,165 | \$ 13,541 | \$ 12,615 | \$ 11,892 | \$ 10,390 | \$ 9,414 | \$ 9,032 | \$ 8,589 | \$ 7,930 | \$ 7,506 |

(1) Retained earnings at the beginning of 1996 was reduced by \$75 million as a result of the adoption of the *Impaired Loans* accounting standard.

(2) Net of related income taxes.

Risk profile

| As at October 31 (\$ millions, except percentage amounts) | 2002 | 2001 | 2000 | 1999 | 1998 | 1997 | 1996 | 1995 | 1994 | 1993 | 1992 |
|--|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|
| Gross impaired loans | | | | | | | | | | | |
| Beginning of year | \$ 2,465 | \$ 1,678 | \$ 1,704 | \$ 2,001 | \$ 1,819 | \$ 2,376 | \$ 2,944 | \$ 4,424 | \$ 7,582 | \$ 7,056 | \$ 3,924 |
| Net additions (reductions) | 1,280 | 1,912 | 813 | 743 | 628 | 81 | 384 | (255) | (1,128) | 1,643 | 3,639 |
| Write-offs and adjustments | (1,457) | (1,125) | (839) | (1,040) | (446) | (638) | (952) | (1,225) | (2,030) | (1,117) | (507) |
| End of year | \$ 2,288 | \$ 2,465 | \$ 1,678 | \$ 1,704 | \$ 2,001 | \$ 1,819 | \$ 2,376 | \$ 2,944 | \$ 4,424 | \$ 7,582 | \$ 7,056 |
| As a % of loans, acceptances and reverse repurchase agreements | 1.0% | 1.1% | .9% | 1.0% | 1.1% | 1.1% | 1.6% | 2.3% | 3.6% | 6.0% | 6.4% |
| Allowance for credit losses | | | | | | | | | | | |
| Specific | \$ 894 | \$ 951 | \$ 747 | \$ 786 | \$ 1,176 | \$ 932 | \$ 1,091 | \$ 1,439 | \$ 1,962 | \$ 2,667 | \$ 1,867 |
| Country risk | — | 31 | 28 | 34 | 40 | 436 | 444 | 930 | 940 | 1,107 | 1,383 |
| General allowance (1) | 1,169 | 1,185 | 863 | 790 | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| General allocated (1) | 251 | 225 | 337 | 290 | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| General unallocated (1) | — | — | — | — | — | — | — | — | — | — | — |
| Total general allowance (1) | 1,420 | 1,410 | 1,200 | 1,080 | 850 | 750 | 700 | 300 | 300 | 550 | 325 |
| Total | \$ 2,314 | \$ 2,392 | \$ 1,975 | \$ 1,900 | \$ 2,066 | \$ 2,118 | \$ 2,235 | \$ 2,669 | \$ 3,202 | \$ 4,324 | \$ 3,575 |
| Composition of allowance | | | | | | | | | | | |
| Allowance for loan losses | \$ 2,203 | \$ 2,278 | \$ 1,871 | \$ 1,884 | \$ 2,026 | \$ 1,769 | \$ 1,875 | \$ 2,003 | \$ 2,559 | \$ 4,255 | \$ 3,575 |
| Allowance for off-balance sheet and other items (2) | 109 | 109 | 98 | — | — | — | — | — | — | — | — |
| Allowance for loan substitute securities | 2 | 5 | 6 | 16 | 40 | 30 | 34 | — | — | — | — |
| Allowance for country risk securities | — | — | — | — | — | 319 | 326 | 666 | 643 | 69 | — |
| Total | \$ 2,314 | \$ 2,392 | \$ 1,975 | \$ 1,900 | \$ 2,066 | \$ 2,118 | \$ 2,235 | \$ 2,669 | \$ 3,202 | \$ 4,324 | \$ 3,575 |
| Allowance for loan losses as a % of loans, acceptances and reverse repurchase agreements | 1.0% | 1.1% | 1.0% | 1.1% | 1.2% | 1.1% | 1.3% | 1.6% | 2.1% | 3.5% | 3.4% |
| Allowance for loan losses as a % of gross impaired loans, excluding LDCs | 96 | 93 | 112 | 112 | 103 | 94 | 77 | 60 | 52 | 52 | 41 |
| Net impaired loans | \$ 83 | \$ 182 | \$ (199) | \$ (196) | \$ (65) | \$ 103 | \$ 524 | \$ 1,148 | \$ 2,093 | \$ 3,258 | \$ 3,481 |
| As a % of loans, acceptances and reverse repurchase agreements | — | .1% | (.1)% | (.1)% | — | .1% | .4% | .9% | 1.7% | 2.7% | 3.3% |
| Provision for credit losses | | | | | | | | | | | |
| Specific | \$ 1,065 | \$ 1,049 | \$ 571 | \$ 530 | \$ 555 | \$ 330 | \$ 340 | \$ 580 | \$ 1,070 | \$ 1,775 | \$ 2,025 |
| Country risk | — | — | — | — | (80) | — | (300) | — | — | (250) | (300) |
| General provision (3) | (22) | 205 | 73 | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| General allocated (3) | 22 | (135) | 47 | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| General unallocated (3) | — | — | — | — | — | — | — | — | — | — | — |
| Total general provision | — | 70 | 120 | 230 | 100 | 50 | 400 | — | (250) | 225 | 325 |
| Total | \$ 1,065 | \$ 1,119 | \$ 691 | \$ 760 | \$ 575 | \$ 380 | \$ 440 | \$ 580 | \$ 820 | \$ 1,750 | \$ 2,050 |
| Specific provisions as a % of average loans, acceptances and reverse repurchase agreements | .51% | .53% | .32% | .30% | .31% | .21% | .26% | .48% | .88% | 1.64% | 1.90% |
| Provision as a % of average loans, acceptances and reverse repurchase agreements | .51 | .56 | .38 | .43 | .32 | .25 | .34 | .48 | .67 | 1.61 | 1.93 |
| Net write-offs | \$ 1,259 | \$ 940 | \$ 677 | \$ 958 | \$ 692 | \$ 528 | \$ 1,001 | \$ 1,105 | \$ 1,979 | \$ 1,187 | \$ 547 |
| As a % of average loans, acceptances and reverse repurchase agreements | .60% | .47% | .38% | .55% | .39% | .34% | .77% | .91% | 1.63% | 1.09% | .51% |

(1) The general allowance was not separated into allocated and unallocated components prior to October 31, 1999.

(2) During 2000, the allowance for off-balance sheet and other items has been separated and reported under Other liabilities. Previously, the amount was included in the allowance for loan losses.

(3) The general provision was not separated into allocated and unallocated components prior to November 1, 1999.

Financial highlights

| (\$ millions, taxable equivalent basis, except per share and percentage amounts) | 2002 | 2001 | 2000 | 1999 | 1998 | 1997 | 1996 | 1995 | 1994 | 1993 | 1992 |
|--|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|
| Performance ratios | | | | | | | | | | | |
| Return on common equity | 15.8% | 16.4% | 19.8% | 15.6% | 18.4% | 19.3% | 17.6% | 16.6% | 16.8% | 2.4% | (.3)% |
| Cash return on common equity (1) | 16.2 | 18.5 | 20.6 | 16.2 | 19.1 | 20.1 | 18.1 | 17.1 | 17.6 | 3.0 | — |
| Return on assets | .75 | .74 | .81 | .65 | .70 | .70 | .70 | .69 | .70 | .21 | .08 |
| Return on assets after preferred dividends | .73 | .70 | .76 | .59 | .64 | .65 | .63 | .60 | .60 | .10 | (.01) |
| Net interest margin (2) | 1.96 | 2.00 | 1.88 | 1.91 | 1.95 | 2.10 | 2.28 | 2.49 | 2.72 | 2.88 | 2.93 |
| Other income as a % of gross revenues | 54.3 | 55.6 | 55.9 | 51.5 | 49.4 | 46.0 | 41.1 | 37.4 | 38.7 | 37.4 | 34.5 |
| Average balances and year-end off-balance sheet data | | | | | | | | | | | |
| Averages | | | | | | | | | | | |
| Assets (3) | \$ 367,300 | \$ 327,100 | \$ 281,900 | \$ 269,900 | \$ 261,300 | \$ 239,500 | \$ 204,900 | \$ 183,800 | \$ 166,700 | \$ 142,500 | \$ 136,200 |
| Loans, acceptances and reverse repurchase agreements | 210,646 | 199,787 | 179,800 | 175,654 | 177,984 | 154,412 | 130,378 | 121,459 | 121,741 | 108,562 | 106,376 |
| Deposits | 240,397 | 218,425 | 193,762 | 184,796 | 178,688 | 166,249 | 147,391 | 136,686 | 133,550 | 114,835 | 108,609 |
| Common equity | 16,809 | 13,843 | 10,814 | 10,264 | 9,107 | 8,003 | 7,320 | 6,627 | 5,964 | 6,052 | 6,313 |
| Total equity | 18,522 | 15,916 | 12,789 | 12,475 | 11,078 | 9,744 | 9,265 | 8,820 | 8,233 | 8,116 | 7,938 |
| Assets under administration (4) | 1,365,900 | 1,342,500 | 1,175,200 | 967,800 | 829,200 | 783,300 | 522,100 | 407,700 | 346,800 | 274,300 | — |
| Assets under management (4) | 90,800 | 100,000 | 92,300 | 81,600 | 73,400 | 67,700 | 51,200 | 40,400 | 39,100 | 33,100 | — |
| Capital ratios | | | | | | | | | | | |
| Tier 1 capital | \$ 15,380 | \$ 14,851 | \$ 13,567 | \$ 12,026 | \$ 11,593 | \$ 10,073 | \$ 9,037 | \$ 8,421 | \$ 7,660 | \$ 6,910 | \$ 6,740 |
| Total capital | 21,012 | 20,171 | 19,044 | 16,698 | 16,480 | 14,705 | 12,069 | 11,913 | 11,525 | 10,941 | 10,483 |
| Total risk-adjusted assets | 165,559 | 171,047 | 158,364 | 149,078 | 157,064 | 147,672 | 128,163 | 121,350 | 120,158 | 117,043 | 114,298 |
| Common equity to risk-adjusted assets | 10.4% | 9.4% | 7.3% | 7.1% | 6.2% | 5.8% | 6.0% | 5.8% | 5.3% | 4.9% | 5.2% |
| Tier 1 capital ratio | 9.3 | 8.7 | 8.6 | 8.1 | 7.4 | 6.8 | 7.0 | 6.9 | 6.4 | 5.9 | 5.9 |
| Total capital ratio | 12.7 | 11.8 | 12.0 | 11.2 | 10.5 | 10.0 | 9.4 | 9.8 | 9.6 | 9.3 | 9.2 |
| Common share information | | | | | | | | | | | |
| Shares outstanding (in thousands) | | | | | | | | | | | |
| End of year | 665,257 | 674,021 | 602,398 | 617,768 | 617,581 | 616,671 | 621,059 | 628,310 | 628,310 | 628,310 | 628,310 |
| Average basic | 672,571 | 641,516 | 606,389 | 626,158 | 617,324 | 617,812 | 628,242 | 628,310 | 628,310 | 628,310 | 621,086 |
| Average diluted | 678,120 | 647,216 | 609,865 | 632,305 | 633,626 | 632,052 | 628,624 | 628,310 | 628,310 | 628,310 | 621,086 |
| Dividends per share | \$ 1.52 | \$ 1.38 | \$ 1.14 | \$ 0.94 | \$ 0.88 | \$ 0.76 | \$ 0.67 | \$ 0.59 | \$ 0.58 | \$ 0.58 | \$ 0.58 |
| Book value per share | 25.91 | 23.95 | 19.10 | 17.17 | 15.81 | 13.96 | 12.20 | 11.21 | 10.06 | 9.04 | 9.41 |
| Share price – High (5) | 58.89 | 53.25 | 48.88 | 42.13 | 46.10 | 38.23 | 22.20 | 15.69 | 15.94 | 14.44 | 14.50 |
| Low (5) | 45.05 | 41.60 | 27.25 | 29.65 | 28.75 | 22.00 | 14.88 | 12.94 | 12.57 | 11.00 | 10.75 |
| Close | 54.41 | 46.80 | 48.30 | 31.73 | 35.55 | 37.68 | 22.15 | 15.07 | 14.19 | 13.63 | 12.07 |
| Price/earnings multiple (6) | 13.2 | 13.5 | 10.8 | 14.2 | 14.0 | 12.2 | 9.0 | 8.2 | 8.9 | — | — |
| Dividend yield (7) | 2.9% | 2.9% | 3.0% | 2.6% | 2.4% | 2.5% | 3.6% | 4.1% | 4.1% | 4.6% | 4.6% |
| Dividend payout ratio (8) | 38 | 39 | 32 | 37 | 32 | 30 | 33 | 34 | 36 | — | — |
| Number of: | | | | | | | | | | | |
| Employees (9) | 59,549 | 57,568 | 49,232 | 51,891 | 51,776 | 48,816 | 46,205 | 49,011 | 49,208 | 52,745 | 49,628 |
| Automated banking machines | 4,486 | 4,548 | 4,517 | 4,585 | 4,317 | 4,248 | 4,215 | 4,079 | 3,948 | 3,981 | 3,828 |
| Service delivery units | | | | | | | | | | | |
| Canada | 1,311 | 1,317 | 1,333 | 1,410 | 1,422 | 1,453 | 1,493 | 1,577 | 1,596 | 1,731 | 1,661 |
| International (10) | 807 | 724 | 306 | 99 | 106 | 105 | 103 | 105 | 97 | 95 | 83 |

- (1) Cash return on common equity is computed by adding back to net income the after-tax amount of amortization of goodwill and other intangibles.
- (2) Net interest income as a percentage of average assets.
- (3) As the information is not reasonably determinable, amounts for years prior to 1995 have not been restated to reflect the presentation of derivative-related amounts on a gross basis.
- (4) Amounts prior to 1996 are as at September 30. Assets under administration and assets under management balances were not reported prior to 1993.
- (5) Intraday high and low share prices.
- (6) Average of high and low common share price divided by diluted earnings per share. The multiples for 1993 and 1992 are not meaningful.
- (7) Dividends per common share divided by the average of high and low share price.
- (8) Common dividends as a percentage of net income after preferred dividends. The ratios for 1993 and 1992 are not meaningful.
- (9) On a full-time equivalent basis.
- (10) International service delivery units include branches, specialized business centres, representative offices and agencies.

Quarterly highlights

| | 2002 | | | | 2001 | | | |
|--|------------|------------|------------|------------|------------|------------|------------|------------|
| | Q4 | Q3 | Q2 | Q1 | Q4 | Q3 | Q2 | Q1 |
| (\$ millions, taxable equivalent basis, except per share and percentage amounts) | | | | | | | | |
| Consolidated statement of income | | | | | | | | |
| Net interest income | \$ 1,815 | \$ 1,768 | \$ 1,746 | \$ 1,869 | \$ 1,784 | \$ 1,719 | \$ 1,580 | \$ 1,466 |
| Other income | 2,043 | 2,104 | 2,192 | 2,223 | 2,255 | 2,008 | 1,924 | 2,028 |
| Provision for credit losses | (235) | (216) | (328) | (286) | (425) | (236) | (210) | (248) |
| Non-interest expense | (2,634) | (2,547) | (2,583) | (2,656) | (2,668) | (2,638) | (2,287) | (2,162) |
| Income taxes | (295) | (385) | (324) | (401) | (262) | (333) | (376) | (401) |
| Non-controlling interest | (28) | (27) | (26) | (27) | (28) | (28) | (29) | (22) |
| Net income | \$ 666 | \$ 697 | \$ 677 | \$ 722 | \$ 656 | \$ 492 | \$ 602 | \$ 661 |
| Cash net income (1) | \$ 683 | \$ 713 | \$ 691 | \$ 739 | \$ 778 | \$ 573 | \$ 651 | \$ 691 |
| Core cash net income (1) | \$ 683 | \$ 713 | \$ 691 | \$ 739 | \$ 539 | \$ 660 | \$ 651 | \$ 613 |
| Earnings per share (2) | | | | | | | | |
| Basic | \$.96 | \$ 1.00 | \$.97 | \$ 1.03 | \$.92 | \$.69 | \$.92 | \$ 1.03 |
| Diluted | .95 | .99 | .96 | 1.03 | .91 | .68 | .92 | 1.02 |
| Cash diluted (1) | .98 | 1.01 | .98 | 1.05 | 1.09 | .81 | 1.00 | 1.07 |
| Core cash diluted (1) | .98 | 1.01 | .98 | 1.05 | .74 | .94 | 1.00 | .95 |
| Performance ratios | | | | | | | | |
| Return on common equity | 14.8% | 15.6% | 16.0% | 16.9% | 15.2% | 12.5% | 18.7% | 20.8% |
| Cash return on common equity (1) | 15.2 | 16.0 | 16.4 | 17.3 | 18.1 | 14.7 | 20.3 | 21.7 |
| Core cash return on common equity (1) | 15.2 | 16.0 | 16.4 | 17.3 | 12.3 | 17.1 | 20.3 | 19.2 |
| Return on assets | .70 | .76 | .76 | .79 | .76 | .58 | .77 | .86 |
| Return on assets after preferred dividends | .67 | .73 | .73 | .76 | .72 | .53 | .72 | .82 |
| Net interest margin (3) | 1.91 | 1.93 | 1.95 | 2.05 | 2.07 | 2.01 | 2.01 | 1.91 |
| Other income as a % of gross revenues | 53.0 | 54.3 | 55.7 | 54.3 | 55.8 | 53.9 | 54.9 | 58.0 |
| Consolidated balance sheet | | | | | | | | |
| Assets | | | | | | | | |
| Cash resources and securities | \$ 115,123 | \$ 111,813 | \$ 107,785 | \$ 101,795 | \$ 98,042 | \$ 93,569 | \$ 86,075 | \$ 80,712 |
| Assets purchased under reverse repurchase agreements | 35,831 | 34,938 | 33,373 | 30,503 | 35,870 | 25,101 | 26,453 | 21,713 |
| Residential mortgages | 72,840 | 70,639 | 70,116 | 69,436 | 67,442 | 66,497 | 64,557 | 63,418 |
| Personal loans | 31,956 | 32,222 | 32,292 | 31,600 | 32,511 | 32,264 | 29,713 | 30,573 |
| Credit card loans | 4,914 | 4,774 | 4,445 | 4,338 | 4,283 | 4,128 | 4,862 | 4,961 |
| Business and government loans | 61,751 | 64,138 | 63,554 | 64,234 | 67,152 | 65,309 | 60,053 | 60,273 |
| Allowance for loan losses | (2,203) | (2,218) | (2,338) | (2,345) | (2,278) | (2,173) | (1,951) | (1,947) |
| Other assets | 56,744 | 57,135 | 47,090 | 54,152 | 56,238 | 45,279 | 43,962 | 42,207 |
| | \$ 376,956 | \$ 373,441 | \$ 356,317 | \$ 353,713 | \$ 359,260 | \$ 329,974 | \$ 313,724 | \$ 301,910 |
| Liabilities and shareholders' equity | | | | | | | | |
| Personal deposits | \$ 101,892 | \$ 101,072 | \$ 99,990 | \$ 100,505 | \$ 101,381 | \$ 98,970 | \$ 93,010 | \$ 90,778 |
| Business, government and bank deposits | 141,594 | 143,383 | 135,888 | 133,659 | 132,066 | 123,321 | 118,326 | 112,344 |
| Other liabilities | 106,604 | 101,628 | 93,377 | 92,773 | 99,656 | 81,268 | 79,321 | 76,704 |
| Subordinated debentures | 6,614 | 7,043 | 7,025 | 7,105 | 6,513 | 6,488 | 6,836 | 6,275 |
| Non-controlling interest in subsidiaries | 1,469 | 1,444 | 1,466 | 1,440 | 1,479 | 1,453 | 1,481 | 1,453 |
| Total equity | 18,783 | 18,871 | 18,571 | 18,231 | 18,165 | 18,474 | 14,750 | 14,356 |
| | \$ 376,956 | \$ 373,441 | \$ 356,317 | \$ 353,713 | \$ 359,260 | \$ 329,974 | \$ 313,724 | \$ 301,910 |
| Selected average balances and off-balance sheet data | | | | | | | | |
| Averages | | | | | | | | |
| Assets | \$ 377,700 | \$ 362,900 | \$ 366,300 | \$ 362,400 | \$ 342,200 | \$ 339,000 | \$ 321,900 | \$ 304,400 |
| Loans, acceptances and reverse repurchase agreements | 217,168 | 208,338 | 207,531 | 209,439 | 205,275 | 205,241 | 197,328 | 191,231 |
| Deposits | 247,258 | 236,918 | 237,479 | 239,838 | 230,292 | 221,167 | 212,813 | 206,975 |
| Common equity | 17,170 | 17,055 | 16,681 | 16,365 | 16,349 | 14,466 | 12,496 | 11,983 |
| Total equity | 18,833 | 18,747 | 18,387 | 18,149 | 18,433 | 16,633 | 14,541 | 14,016 |
| Assets under administration | 1,365,900 | 1,413,100 | 1,442,800 | 1,426,600 | 1,342,500 | 1,271,800 | 1,198,700 | 1,242,800 |
| Assets under management | 90,800 | 94,200 | 96,200 | 103,300 | 100,000 | 110,500 | 110,400 | 112,500 |
| Provision for credit losses | | | | | | | | |
| Specific | \$ 235 | \$ 216 | \$ 328 | \$ 286 | \$ 425 | \$ 236 | \$ 210 | \$ 178 |
| General provision | | | | | | | | |
| General allocated | (15) | 4 | - | (11) | 108 | - | - | 97 |
| General unallocated | 15 | (4) | - | 11 | (108) | - | - | (27) |
| Total general provision | - | - | - | - | - | - | - | 70 |
| Total | \$ 235 | \$ 216 | \$ 328 | \$ 286 | \$ 425 | \$ 236 | \$ 210 | \$ 248 |
| Net impaired loans as a % of loans, acceptances and reverse repurchase agreements | .04% | .07% | .09% | .18% | .08% | .01% | .02% | (.11)% |
| Capital ratios | | | | | | | | |
| Common equity/risk-adjusted assets | 10.4% | 10.2% | 10.0% | 9.8% | 9.4% | 9.5% | 8.0% | 7.6% |
| Tier 1 | 9.3 | 9.1 | 9.0 | 8.8 | 8.7 | 9.3 | 8.8 | 8.3 |
| Total | 12.7 | 12.7 | 12.6 | 12.3 | 11.8 | 12.3 | 12.3 | 11.5 |
| Common share information | | | | | | | | |
| Shares outstanding (in thousands) | | | | | | | | |
| End of period | 665,257 | 671,671 | 673,860 | 673,596 | 674,021 | 683,312 | 616,516 | 616,209 |
| Average basic | 668,868 | 673,787 | 673,751 | 674,465 | 681,758 | 658,296 | 616,365 | 608,824 |
| Average diluted | 674,840 | 679,168 | 678,751 | 679,729 | 687,334 | 663,996 | 621,907 | 614,686 |
| Dividends per share | \$.40 | \$.38 | \$.38 | \$.36 | \$.36 | \$.36 | \$.33 | \$.33 |
| Book value per share | 25.91 | 25.56 | 25.04 | 24.53 | 23.95 | 23.68 | 20.61 | 20.01 |
| Common share price - High (4) | 57.55 | 58.89 | 57.07 | 52.45 | 53.25 | 51.50 | 51.25 | 52.80 |
| Low (4) | 48.80 | 45.05 | 46.36 | 46.81 | 41.60 | 42.80 | 42.42 | 45.10 |
| Close | 54.41 | 53.45 | 54.97 | 50.00 | 46.80 | 50.96 | 42.95 | 48.20 |
| Dividend yield | 3.0% | 2.9% | 2.9% | 2.9% | 3.0% | 3.1% | 2.8% | 2.7% |
| Dividend payout ratio | 41% | 38% | 39% | 35% | 39% | 54% | 36% | 32% |

(1) Cash net income, cash diluted earnings per share and cash return on common equity are computed by adding back to net income the after-tax amount of amortization of goodwill and other intangibles. Further deducting the impact of special items results in core cash net income, core cash diluted earnings per share and core cash return on common equity.

(2) Earnings per share for the year may not equal the sum of the quarters.

(3) Net interest income as a percentage of average assets.

(4) Intraday high and low share price.

Glossary

Acceptances

A bill of exchange or negotiable instrument drawn by the borrower for payment at maturity and accepted by a bank. The acceptance constitutes a guarantee of payment by the bank and can be traded in the money market. The bank earns a “stamping fee” for providing this guarantee.

Allowance for credit losses

The amount deemed adequate by management to absorb identified and probable credit related losses in the portfolio of loans, acceptances, guarantees, letters of credit, deposits with other banks and derivatives. The allowance is increased by the provision for credit losses, which is charged to income and decreased by the amount of charge-offs (write-offs in Canadian GAAP), net of recoveries.

Assets under administration (AUA)

Assets administered by a financial institution which are beneficially owned by clients and are therefore not reported on the consolidated balance sheet. Services provided in respect of assets under administration are of an administrative nature, including safekeeping, collecting investment income, settling purchase and sale transactions, and record keeping.

Assets under management (AUM)

Asset managed by a financial institution which are beneficially owned by clients and are therefore not reported on the consolidated balance sheet. Services provided in respect of assets under management include the selection of investments and the provision of investment advice. Assets under management may also be administered by the financial institution.

Basis point (bp)

One one-hundredth of a percentage point (.01%).

Beta

The measure of a security's volatility relative to a market index.

Canadian GAAP

Canadian generally accepted accounting principles.

Capital ratio (Canadian basis)

The percentage of risk-adjusted assets supported by capital using the guidelines of the Superintendent of Financial Institutions Canada based on standards issued by the Bank for International Settlements and Canadian GAAP financial information.

Capital ratio (U.S. basis)

The percentage of risk-adjusted assets supported by capital using the guidelines issued to U.S. banks by the Board of Governors of the Federal Reserve System and U.S. GAAP financial information.

Commercial clients

Generally, mid-market private companies with sophisticated financial needs (e.g., financing requirements between \$5 million and \$100 million), served by our RBC Banking segment. Large corporations with a frequent need to access capital markets and greater financing requirements are served by RBC Capital Markets.

Commitments to extend credit

Credit facilities available to clients either in the form of loans, bankers' acceptances and other on-balance sheet financing, or through off-balance sheet products such as guarantees and letters of credit.

Cost of capital

Management's estimate of its weighted average cost of equity and debt capital.

Derivative

A derivative is a contract whose value is “derived” from interest rates, foreign exchange rates, or equity or commodity prices. Use of derivatives allows for the transfer, modification or reduction of current or expected risks, including interest rate, foreign exchange and other market risks. The most common types of derivatives include interest rate and cross currency swaps, foreign exchange forward contracts, foreign currency and interest rate futures, forward rate agreements, and foreign currency and interest rate options. Derivatives can be transacted either through organized exchanges or over-the-counter agreements.

Dividend payout ratio

Common dividends as a percentage of net income after preferred share dividends.

Dividend yield

Dividends per common share divided by the average of the high and low share prices.

Documentary and commercial letters of credit

Written undertakings by a bank on behalf of its client (typically an importer), authorizing a third party (e.g., an exporter) to draw drafts on the bank up to a stipulated amount under specific terms and conditions. Such undertakings are established for the purpose of facilitating international trade.

Earnings per share, basic

Net income less preferred share dividends divided by the average number of shares outstanding.

Earnings per share (EPS), diluted

Net income less preferred share dividends divided by the average number of shares outstanding adjusted for the dilutive effects of stock options and other convertible securities.

Economic Capital (EC)

EC is an estimate of the amount of equity capital required to underpin risks. It is calculated by estimating the level of capital that is necessary to support our various businesses, given their risks, consistent with our desired solvency standard and credit ratings.

Economic Profit

Economic Profit is cash operating earnings (i.e., net income available to common shareholders excluding the after-tax impact of special items and amortization of goodwill and other intangibles) less a charge for the estimated cost of common equity.

Efficiency ratio

Non-interest expenses expressed as a percentage of gross revenue (i.e., net interest income and non-interest revenue). Used as a measure of productivity and for comparison with peers.

Foreign exchange spot and forward contract

A foreign exchange forward contract, which is a type of derivative, is a commitment to buy or sell a fixed amount of foreign currency on a future specified date at a set rate of exchange. A foreign exchange spot contract is a commitment to buy or sell a fixed amount of foreign currency for delivery within two business days of the contract date.

Forward rate agreement (FRA)

A contract which obliges two parties to make a cash settlement at a future date for the difference between a contracted rate of interest and the current market rate, based on a notional amount.

Futures

A contract which creates an obligation to buy or sell a foreign currency or a financial instrument on a future date at a specified price established on a commodity exchange.

Goodwill/Amortization of goodwill

Goodwill represents the excess of the price paid for the acquisition of subsidiaries over the fair value of the net assets acquired, and up to the end of 2001, was amortized over appropriate periods of up to 20 years, except where a writedown was required to reflect permanent impairment. Effective November 1, 2001, as a result of a change in accounting standards, goodwill is no longer amortized but is tested for impairment at a reporting unit level on a periodic basis.

Guarantees and standby letters of credit

Primarily represent irrevocable assurances that a bank will make payments in the event that its client cannot meet its financial obligations to third parties. Certain other guarantees, such as bid and performance bonds, represent non-financial undertakings.

Hedge

A risk management technique used to insulate financial results from market, interest rate or foreign currency exchange risk (exposure) arising from normal banking operations. The elimination or reduction of such exposure is accomplished by establishing offsetting positions. For example, assets denominated in foreign currencies can be offset with liabilities in the same currencies or through the use of foreign exchange hedging instruments such as futures, options or foreign exchange contracts.

International

In the context of the annual report, the term international refers to Royal Bank of Canada's operations and clients outside of Canada.

Mark-to-market

Valuation at market rates, as of the balance sheet date, of securities and derivatives held for trading purposes.

Net interest income

The difference between what is earned on assets such as loans and securities and what is paid on liabilities such as deposits and subordinated debentures.

Net interest margin

Net taxable equivalent interest income divided by average interest-earning assets. It is a measure of how effectively a corporation utilizes its earning assets in relation to its sources of funding.

Nonaccrual loans/Impaired loans

Loans are classified as nonaccrual (impaired in Canadian GAAP) when, in the opinion of management, there is no longer reasonable assurance of the timely collection of principal and interest. Loans, other than credit card balances and government guaranteed loans, are automatically classified as nonaccrual when a payment is 90 days past due, unless the loan is well secured and in the process of collection.

Notional amount

The contract amount used as a reference point to calculate payments for derivatives.

Off-balance sheet financial instrument

A variety of products offered to clients which fall into two broad categories: (i) credit related arrangements which generally provide clients with liquidity protection, and (ii) derivatives, which are defined on the previous page.

Operating efficiency ratio

Operating non-interest expenses as a percentage of operating revenues.

Operating non-interest expenses

Non-interest expenses excluding special items, costs of Stock Appreciation Rights and certain acquisition expenses such as retention compensation.

Operating revenues

Revenues excluding special items.

Options (foreign currency, interest rate)

A contract in which the writer grants the purchaser the right, but not the obligation, either to buy (call option) or sell (put option) at or by a set date a set amount of foreign currency or a financial instrument at a set price.

Prepaid pension costs

The cumulative excess of amounts contributed to a pension fund over the amounts recorded as pension expense.

Provision for credit loss

The amount charged to income necessary to bring the allowance for credit losses to a level determined appropriate by management.

Repurchase agreements (REPOS)

Involve the sale of securities for cash at a near value date and the simultaneous repurchase of the securities for value at a later date.

Return on equity (ROE)

Net income, less preferred share dividends, expressed as a percentage of average common equity.

Reverse repurchase agreements (reverse REPOS)

Involve the purchase of securities for cash at a near value date and the simultaneous sale of the securities for value at a later date.

Risk

Financial institutions face a number of different risks that expose them to possible losses. These risks include credit risk, market risk, liquidity risk, insurance risk and operational risk.

Risk-adjusted assets

Used in the calculation of risk-based capital ratios. The face value of assets is discounted using risk-weighting factors in order to reflect a comparable risk per dollar among all types of assets. The risk inherent in off-balance sheet instruments is also recognized, first by adjusting notional values to balance sheet (or credit) equivalents, and then by applying appropriate risk-weighting factors.

Securities lending

Transactions in which a bank acts as an agent for the owner of a security, who agrees to lend the security under the terms of a pre-arranged contract to a borrower for a fee. The borrower must fully collateralize the security loan at all times. There are two types of securities lending arrangements, lending with and without credit or market risk indemnification. In securities lending without indemnification, the bank bears no risk of loss. For transactions in which the bank provides an indemnification, risk of loss occurs if the borrower defaults and the value of the collateral declines concurrently.

Securities sold short

A transaction in which the seller sells securities it does not own. The seller borrows the securities in order to deliver them to the purchaser. At a later date, the seller buys identical securities in the market to replace the borrowed securities.

Securitization

The process by which high-quality assets, mainly loans or mortgages, are pooled into standardized securities backed by these assets, which can be traded.

Special items

Items that are viewed by management as items that do not arise as part of normal day-to-day business operations or that are unusual in nature and could potentially distort the calculation of trends analyzed by management.

Special purpose entities (SPEs)

SPEs are entities that are typically organized for a single discrete purpose, have a limited life and serve to legally isolate the financial assets held by the SPE from the selling organization. SPEs are principally used to securitize financial and other assets in order to obtain access to funding, to mitigate credit risk and to manage capital.

Stock Appreciation Rights (SARs)

Rights attached to stock options, which can be exchanged for a cash amount equal to the difference between the exercise price and the closing price of common shares on the day immediately preceding the day of exercise.

Superintendent of Financial Institutions (OSFI)

The primary regulator of federally chartered financial institutions and federally administered pension plans in Canada. OSFI's mission is to safeguard policyholders, depositors and pension plan members from undue loss.

Swaps (foreign currency, interest rate)

Contracts which oblige two parties to exchange currencies and/or the related interest flows (e.g., fixed-rate for floating-rate) on a specified notional amount for a specified period.

Taxable equivalent adjustment

An addition to interest income in order to gross up the tax-exempt income earned on certain securities (primarily loan substitute securities) to an amount which, had it been taxable at the statutory rate, would result in the same after-tax net income as appears in the financial statements. The gross-up of such income to a taxable equivalent basis permits a uniform measurement and comparison of net interest income.

Trust Capital Securities (RBC TruCS)

A form of innovative Tier 1 capital which is reported as a non-controlling interest in a subsidiary on the consolidated balance sheet.

U.S. GAAP

U.S. generally accepted accounting principles.

Value-At-Risk (VAR)

A generally accepted risk-measurement concept that uses statistical models to estimate within a given level of confidence the maximum loss in market value that the bank would experience in its trading portfolios from an adverse one-day movement in market rates and prices.

Directors and executive officers

Directors

| | | | |
|---|--|--|---|
| W. Geoffrey Beattie (2001) <i>Toronto</i> President The Woodbridge Company Limited Deputy Chairman The Thomson Corporation | The Hon. Paule Gauthier , P.C., O.C., O.Q., Q.C. (1991) <i>Quebec City</i> Senior Partner Desjardins Ducharme Stein Monast | Charlotte R. Otto (2000) <i>Cincinnati, Ohio</i> Global External Relations Officer The Procter & Gamble Company | Cecil W. Sewell, Jr. (2001) <i>Raleigh, North Carolina</i> Chairman Emeritus RBC Centura Banks, Inc. |
| George A. Cohon , O.C., O.Ont. (1988) <i>Toronto</i> Founder and Senior Chairman McDonald's Restaurants of Canada Limited | Brandt C. Louie , F.C.A. (2001) <i>West Vancouver</i> President and Chief Executive Officer H.Y. Louie Co. Limited Chairman and Chief Executive Officer London Drugs Limited | Robert B. Peterson (1992) <i>Toronto</i> Company Director | Kathleen P. Taylor (2001) <i>Toronto</i> President, Worldwide Business Operations Four Seasons Hotels Inc. |
| Douglas T. Elix (2000) <i>Ridgefield, Connecticut</i> Senior Vice-President and Group Executive IBM Global Services IBM Corporation | J. Edward Newall , O.C. (1984) <i>Calgary</i> Chairman of the Board NOVA Chemicals Corporation Chairman of the Board Canadian Pacific Railway Limited | J. Pedro Reinhard (2000) <i>Midland, Michigan</i> Executive Vice-President and Chief Financial Officer The Dow Chemical Company | Victor L. Young , O.C. (1991) <i>St. John's</i> Company Director |
| John T. Ferguson , F.C.A. (1990) <i>Edmonton</i> Chairman of the Board Princeton Developments Ltd. Chair of the Board TransAlta Corporation | Gordon M. Nixon (2001) <i>Toronto</i> President and Chief Executive Officer Royal Bank of Canada | Hartley T. Richardson (1996) <i>Winnipeg</i> President and Chief Executive Officer James Richardson & Sons, Limited | The date appearing after the name of each director indicates the year in which the individual became a director. The term of office of each director will expire at the next Annual Meeting of Shareholders on February 28, 2003. |
| L. Yves Fortier , C.C., Q.C. (1992) <i>Montreal</i> Chairman Ogilvy Renault Chairman of the Board Alcan Inc. | David P. O'Brien (1996) <i>Calgary</i> Chairman of the Board EnCana Corporation | Kenneth C. Rowe , F.C.I.S. (1985)* <i>Halifax</i> Chairman and Chief Executive Officer I.M.P. Group International Inc. | |
| | | Guy Saint-Pierre , O.C. (1990) <i>Montreal</i> Chairman of the Board Royal Bank of Canada | |

Executive officers – Group Management Committee

| | | | |
|---|---|--|--|
| Elisabetta Bigsby ** Senior Executive Vice-President Human Resources & Public Affairs | Martin J. Lippert Vice-Chairman RBC Global Services & Chief Information Officer | James T. Rager Vice-Chairman RBC Banking | W. James Westlake Chairman & Chief Executive Officer RBC Insurance |
| Peter W. Currie Vice-Chairman & Chief Financial Officer | W. Reay Mackay Vice-Chairman RBC Investments | Irving Weiser Chairman & Chief Executive Officer RBC Dain Rauscher | Charles M. Winograd Vice-Chairman RBC Capital Markets |
| Suzanne B. Labarge Vice-Chairman & Chief Risk Officer | Gordon M. Nixon President & Chief Executive Officer | | |

** Effective December 2, 2002.

Corporate governance

Our corporate governance policies are designed to support the ability of the Board of Directors to supervise management and to enhance long-term shareholder value.

The board's strengths include an independent chairman, and knowledgeable, well-informed directors who give priority to strategic planning, ensure that standards exist to promote ethical behaviour throughout the organization, and seek continuous improvement in corporate governance practices.

Our system of governance is consistent with the Toronto Stock Exchange's guidelines for effective corporate governance (the TSX Guidelines), including revisions to the TSX Guidelines that were proposed in the spring of 2002 but were not formally implemented as of October 31, 2002.

The board has been reviewing its practices in response to the United States *Sarbanes-Oxley Act of 2002* (SOX), as well as the New York Stock Exchange's corporate governance rule proposals (the NYSE Proposals). As provisions of SOX and the NYSE Proposals come into effect, the board will continue to review and amend its governance practices on an ongoing basis to respond to these standards.

The Management Proxy Circular issued in connection with the 2003 Annual Meeting contains a comparison of the bank's governance procedures with the TSX Guidelines and with certain NYSE Proposals, which differ from or are in addition to the TSX Guidelines.

Responsibilities: The board has a written mandate setting out its key functions, which include succession planning, evaluating management performance, reviewing strategy and major business decisions, reviewing and approving corporate financial goals and the operating plan, identifying risks, overseeing communications and public disclosure, and assessing the effectiveness of the bank's internal controls and management information systems. The board specifies those matters that require its approval and delegates others to management.

Composition: The board derives its strength from the background, diversity, qualities, skills and experience of its members. With advice from outside consultants, the Corporate Governance and Public Policy Committee recommends to the board candidates suitable for nomination. Nominees are selected for qualities such as integrity, business judgment, independence, business or professional expertise, international experience, residency and familiarity with geographic regions relevant to the bank's strategic priorities.

As of November 19, 2002, there were 19 directors. At the Annual Meeting, 18 directors will be elected. The Corporate Governance and Public Policy Committee reviews the composition and mandates of the board's four committees. Mandates and activities of the board committees are summarized on page 107.

Independence: An independent director, Mr. Guy Saint-Pierre, acts both as Chairman of the Board and as Chair of the Corporate Governance and Public Policy Committee. Following every board meeting, the Chairman chairs sessions attended only by non-management directors.

Board policy permits no more than two board members from management. Currently two directors, the President and Chief Executive Officer of the bank and the Chairman Emeritus of RBC Centura Banks, Inc., are from management.

We comply with provisions of the *Bank Act* and the TSX Guidelines with regard to directors being "affiliated" with or "related" to the bank. Only 2 of the 18 persons proposed for election to the board at the Annual Meeting are "related" to the bank. This is well within the limits required by the *Bank Act* and TSX Guidelines.

Committees of the board consist solely of non-management directors. All members of the Audit Committee are "unrelated" to the bank and a majority of the members of each other committee are "unrelated".

The Corporate Governance and Public Policy Committee is developing categorical standards of "independence" to apply to members of the board and its committees in addition to the "affiliated" and "related" standards. It is anticipated that following this Annual Meeting, all members of the Audit Committee, the Corporate Governance and Public Policy Committee, and the Human Resources Committee will be "unrelated" under the Canadian standards and "independent" under the U.S. standards.

Information: The board has timely access to the information it needs to carry out its duties. Directors help set the agenda for board and committee meetings, receive a comprehensive package of information prior to each board and committee meeting, and attend an annual strategy planning session. As well, after each committee meeting, the full board receives a report on the committee's work. An ongoing education program and a Director's Guide, focusing on roles and responsibilities of board members, are provided for directors.

Ethical Behaviour: Our Code of Conduct and related policies are reviewed by the board and set high standards for ethical behaviour throughout the organization.

The Code of Conduct provides the entire organization with the same frame of reference for dealing with sensitive and complex issues. It incorporates guiding principles such as upholding the law, confidentiality, integrity and individual responsibility, and provides for accountability if employees fail to meet the Code's standards.

The board has approved the establishment and mandate of an Ethics and Compliance Committee, composed of senior management. This committee has responsibility for ensuring that our policies and management systems are appropriately implemented to ensure adherence to the principles outlined in the Code of Conduct.

Communications: We are committed to excellence and timeliness in our communications. The investor relations staff provides information to current and potential investors and responds to their inquiries. It is our policy that every shareholder inquiry receives a prompt response from an appropriate officer. Senior executives, including the President and Chief Executive Officer, Chief Financial Officer and Senior Vice-President, Investor Relations, meet regularly with financial analysts and institutional investors. The quarterly earnings conference calls with analysts and institutional investors are broadcast live and archived on the Internet and are accessible on a live and recorded basis via telephone to interested retail investors, the media and members of the public for a period of three months after each call. Presentations at investor conferences are promptly made available on the Internet or via telephone. We also make significant disclosure documents available on the investor relations Web site at: rbc.com/investorrelations.

Subsidiary Governance Office (SGO): Last year the SGO was launched to enhance and harmonize governance in our many subsidiaries. System-wide installation of sophisticated software technology allows quick and easy access to up-to-date information on all parts of our global network. Other benefits include consistent governance oversight, which mitigates both the risk of loss due to governance failure and the risk of non-compliance with regulation. The launch of the SGO has also paved the way for a thorough review of each business, leading to a streamlining of the corporate organization, which will yield a more economical and sharply focused group structure.

Summary of Mandates and Activities of Board Committees

The board delegates certain work to board committees. This allows in-depth analysis of issues by the committees and more time for the full board to discuss and debate items of business. Each committee annually evaluates its effectiveness in carrying out its mandate.

Audit Committee

- Reviews matters prescribed by the *Bank Act*, including annual and quarterly financial statements, and returns specified by the Superintendent of Financial Institutions Canada
- At least quarterly, meets separately with the external auditors, the Chief Internal Auditor and senior management to discuss any matters they deem appropriate
- Recommends to the shareholders the appointment of the external auditors and has sole authority to approve all audit engagement fees and terms as well as the provision of any non-audit services provided by the external auditors
- Oversees the work of the external auditors, including resolution of disagreements between management and the external auditors regarding financial reporting, and reviews with the external auditors any audit problems or difficulties and management's response
- Reviews with the external auditors the external audit plan, the results of the audit, and the qualifications, independence and objectivity of the external auditors, including formal written statements delineating relationships between the external auditors and the bank that may impact on such independence and objectivity, and recommends actions that the board should take to satisfy itself of the independence of the external auditors
- Requires management to implement and maintain appropriate systems of internal control and meets with the Chief Internal Auditor and management to assess the adequacy and effectiveness of those systems
- Reviews the annual internal audit plan and duties, responsibilities, performance, objectivity and staffing of the internal audit function
- Reviews the mandate of and concurs in the appointment of the Chief Internal Auditor and meets with the Chief Internal Auditor to review any significant issues reported to management and management's responses to any such reports
- Reviews investments and transactions that could adversely affect the well-being of the bank, reports on significant litigation and regulatory compliance matters and prospectuses relating to the issue of securities of the bank
- Reviews internal controls and the control environment and policies related to liquidity management and capital management in compliance with the Canada Deposit Insurance Corporation Standards of Sound Business and Financial Practices (the CDIC Standards)

Members: J.T. Ferguson, J.E. Newall, R.B. Peterson (Chair), J.P. Reinhard, K.P. Taylor, V.L. Young

Conduct Review and Risk Policy Committee

- Reviews credits to directors or entities in which they are partners, directors or officers
- Approves delegation of risk limits to management and any transactions exceeding this delegated authority
- Reviews risk reporting on significant risks, including the amount, nature, characteristics, concentration and quality of the bank's credit portfolio, as well as all significant exposures to credit risk
- Establishes investment and lending policies, standards and procedures
- Reviews standards of business conduct and ethical behaviour for the bank's directors, senior management and employees
- Reviews risk management policies and processes concerning significant risks (credit, market, structural, fiduciary and operational) in compliance with CDIC Standards
- Reviews bank procedures for complying with self-dealing provisions of the *Bank Act*
- Establishes and monitors procedures for restricting the use of confidential information, dealing with complaints, disclosing information to clients and resolving conflicts of interest

Members: J.T. Ferguson (Chair), L.Y. Fortier, P. Gauthier, B.C. Louie, H.T. Richardson, K.C. Rowe

Corporate Governance and Public Policy Committee

- Makes recommendations regarding the effectiveness of the system of corporate governance, including the board program and forward agenda for board and committee meetings, the frequency and content of meetings, the need for any special meetings, communication processes between the board and management, mandates of board committees and policies governing size and composition of the board
- Assesses the performance of the board, including its committees, and monitors directors' performance. As part of this process, directors evaluate in writing the performance of the board and its committees, and the resulting data is analyzed by an independent outside consultant
- Reviews the credentials of directors standing for re-election
- Identifies and recommends to the board candidates suitable for nomination as directors, with sole authority to retain and approve the fees of any search firm to be used to identify director candidates
- Reviews shareholder proposals and recommends to the board the bank's response to the proposals
- Advises management in the planning of the annual strategy meeting attended by directors and senior management
- Reviews the amount and form of compensation of directors and, based on a report from an independent outside consultant, recommends appropriate adjustments
- Reviews whether the conduct of the bank's business is ethical and socially responsible
- Oversees the bank's communications policy, including processes for communicating with clients, employees, shareholders and the community
- Reviews policies designed to create a positive corporate image
- Reviews the bank's policy on and budget for political donations
- Reviews the charitable contributions policy and budget

Members: G.A. Cohon, L.Y. Fortier, J.E. Newall, D.P. O'Brien, C.R. Otto, G. Saint-Pierre (Chair)

Human Resources Committee

- Annually approves the Code of Conduct for directors and employees
- Reviews and approves principles for employee recruitment and hiring
- Reviews management succession plans for executive officers of the bank and its business groups
- Reviews major compensation policies and recommends incentive programs and equity-based compensation plans to the board
- Reviews the bank's major compensation programs against its business objectives and operations and the risks to which it is exposed, and its adherence to its processes, policies, procedures and controls
- In consultation with the Corporate Governance and Public Policy Committee, annually evaluates the non-executive Chairman
- Reviews the position description for the CEO and annually evaluates the CEO's performance against approved corporate objectives
- Recommends to the board the remuneration of the CEO and certain other senior executives and has sole authority to retain and approve the fees of any compensation consultant to assist in evaluating that remuneration
- Advises the board on policy with respect to the administration, funding and investment of the pension plans and reviews the bank's pension plan performance and funded status
- Approves an annual report on executive compensation for inclusion in the management proxy circular

Members: W.G. Beattie, D.T. Elix, P. Gauthier, D.P. O'Brien (Chair), R.B. Peterson, G. Saint-Pierre

Principal subsidiaries

| Principal subsidiaries (1) | Principal office address (2) | Carrying value of voting shares owned by the bank (3) |
|---|-------------------------------------|---|
| Royal Bank Mortgage Corporation (4) | Montreal, Quebec, Canada | \$ 898 |
| Royal Trust Corporation of Canada (4) | Toronto, Ontario, Canada | 771 |
| The Royal Trust Company | Montreal, Quebec, Canada | 469 |
| Royal Mutual Funds Inc. | Toronto, Ontario, Canada | 3 |
| RBC Capital Trust | Toronto, Ontario, Canada | 506 |
| Connor Clark Ltd. | Toronto, Ontario, Canada | 38 |
| RBC Action Direct Inc. | Richmond Hill, Ontario, Canada | 135 |
| RBC Alternative Assets, L.P. (2), (5) | New York, New York, U.S.A. | 14 |
| RBC Technology Ventures, Inc. | Toronto, Ontario, Canada | 33 |
| RBC Capital Partners Limited | Toronto, Ontario, Canada | 50 |
| Royal Bank Holding Inc. | Toronto, Ontario, Canada | 14,670 |
| RBC Insurance Holdings Inc. | Mississauga, Ontario, Canada | |
| RBC Life Insurance Company | Mississauga, Ontario, Canada | |
| RBC Dominion Securities Limited (4) | Toronto, Ontario, Canada | |
| RBC Dominion Securities Inc. | Toronto, Ontario, Canada | |
| RBC Alternative Assets, Inc. (2), (5) | New York, New York, U.S.A. | |
| Royal Bank Realty Inc. | Montreal, Quebec, Canada | |
| R.B.C. Holdings (Bahamas) Limited | Nassau, Bahamas | |
| Royal Bank of Canada Reinsurance (Cayman) Limited | George Town, Grand Cayman | |
| Royal Bank of Canada Insurance Company Ltd. | St. Michael, Barbados | |
| Finance Corporation of Bahamas Limited | Nassau, Bahamas | |
| Investment Holdings (Cayman) Limited | George Town, Grand Cayman | |
| Royal Bank of Canada (Barbados) Limited | St. Michael, Barbados | |
| Royal Bank of Canada (Caribbean) Corporation | St. Michael, Barbados | |
| RBC Holdings (USA) Inc. | New York, New York, U.S.A. | |
| RBC Dain Rauscher Corp. (2) | Minneapolis, Minnesota, U.S.A. | |
| RBC Dominion Securities Corporation | New York, New York, U.S.A. | |
| RBC Insurance Holdings (USA) Inc. (2) | Wilmington, Delaware, U.S.A. | |
| Liberty Life Insurance Company | Greenville, South Carolina, U.S.A. | |
| RBC Holdings (Delaware) Inc. (6) | New York, New York, U.S.A. | |
| Prism Financial Corporation | Chicago, Illinois, U.S.A. | |
| RBC Mortgage Company | Chicago, Illinois, U.S.A. | |
| RBC Centura Banks, Inc. | Rocky Mount, North Carolina, U.S.A. | 3,590 |
| RBC Centura Bank (6) | Rocky Mount, North Carolina, U.S.A. | |
| RBC Capital Investment Holdings (USA) Inc. | Wilmington, Delaware, U.S.A. | 69 |
| Royal Bank of Canada Financial Corporation | St. Michael, Barbados | 4 |
| Atlantis Holdings Limited | St. Michael, Barbados | 489 |
| RBC Finance B.V. | Amsterdam, Netherlands | 2,329 |
| Royal Bank of Canada Holdings (U.K.) Limited | London, England | |
| Royal Bank of Canada Europe Limited | London, England | |
| RBC Holdings (Channel Islands) Limited | Guernsey, Channel Islands | |
| Royal Bank of Canada (Channel Islands) Limited | Guernsey, Channel Islands | |
| RBC Investment Management (Asia) Limited | Hong Kong, China | 5 |
| RBC Global Services Australia Pty Limited | Sydney, New South Wales, Australia | 48 |

(1) The bank owns 100% of the voting shares of each subsidiary, except Finance Corporation of Bahamas Limited (75%).

(2) Each subsidiary is incorporated under the laws of the state or country in which the principal office is situated, except for RBC Alternative Assets Inc., RBC Alternative Assets, L.P., RBC Holdings (USA) Inc., RBC Dain Rauscher Corp. and Prism Financial Corporation, which are incorporated under the laws of the state of Delaware, U.S.A.

(3) The carrying value (in millions of dollars) of voting shares is stated as the bank's equity in such investments.

(4) The subsidiaries have outstanding non-voting shares of which the bank, directly or indirectly, owns 100%.

(5) RBC Alternative Assets, Inc. owns 1.1% of RBC Alternative Assets, L.P.

(6) RBC Holdings (Delaware) Inc. owns 2.4% of RBC Centura Banks, Inc.

Shareholder information

Corporate headquarters

Street address:
Royal Bank of Canada
200 Bay Street
Toronto, Ontario, Canada
Tel: (416) 974-5151
Fax: (416) 955-7800

Mailing address:
P.O. Box 1
Royal Bank Plaza
Toronto, Ontario
Canada M5J 2J5

Web site:
rbc.com

Transfer Agent and Registrar

Main Agent
Computershare Trust
Company of Canada

Street address:
1500 University Street
Suite 700
Montreal, Quebec
Canada H3A 3S8
Tel: (514) 982-7888, or
1-866-586-7635
Fax: (514) 982-7635

Mailing address:
P.O. Box 1570, Station "B"
Montreal, Quebec
Canada H3B 3L2

Web site:
computershare.com

Co-Transfer Agent (U.S.)

The Bank of New York
101 Barclay Street
New York, New York
U.S. 10286

Co-Transfer Agent (United Kingdom)

Computershare Services PLC
Securities Services – Registrars
P.O. Box No. 82, The Pavilions,
Bridgwater Road, Bristol
BS99 7NH England

Stock exchange listings

(Symbol: RY)

Common shares are listed on:
Canada
Toronto Stock Exchange (TSX)
U.S.
New York Stock Exchange (NYSE)
Switzerland
Swiss Exchange (SWX)

All preferred shares are listed
on the Toronto Stock Exchange.

Valuation Day price

For capital gains purposes, the
Valuation Day (December 22,
1971) cost base for the bank's
common shares is \$7.38 per
share. This amount has been
adjusted to reflect the two-for-one
share split of March 1981 and the
two-for-one share split of February
1990. The one-for-one share divi-
dend paid in October 2000 did
not affect the Valuation Day value
for the bank's common shares.

Shareholder contact

For information about stock
transfers, address changes,
dividends, lost stock certificates,
tax forms, estate transfers,
contact: Computershare Trust
Company of Canada
1500 University Street,
Suite 700
Montreal, Quebec
Canada H3A 3S8
Tel: (514) 982-7888 or
1-866-586-7635.

For other shareholder inquiries,
contact: Investor Relations
Royal Bank of Canada
123 Front Street West,
6th Floor
Toronto, Ontario
Canada M5J 2M2
Tel: (416) 955-7806
or visit our Web site at:
rbc.com/investorrelations.

2003 Annual Meeting

The bank's next Annual Meeting
of Common Shareholders will
be held on Friday, February 28,
2003 at 9:30 a.m. (EST) in the
Auditorium at the Mount Royal
Centre, 2200 Mansfield Street,
Montreal, Quebec, Canada.

2003 quarterly earnings release dates

| | |
|----------------|---------|
| First quarter | Feb. 28 |
| Second quarter | May 30 |
| Third quarter | Aug. 26 |
| Fourth quarter | Nov. 25 |

Direct deposit service

Shareholders may have their
dividends deposited by electronic
funds transfer directly to an
account at any financial institu-
tion that is a member of the
Canadian Payments Association.
To arrange for this, please contact
Computershare Trust Company of
Canada at their mailing address.

Dividend dates for 2003

Subject to approval by the Board of Directors.

| | Record dates | Payment dates |
|--|--|---|
| Common and preferred shares series J, K, N, O, P and S | Jan. 27 Apr. 23 Jul. 23 Oct. 27 | Feb. 24 May 23 Aug. 22 Nov. 24 |

Credit ratings

(as at December 10, 2002)

| | Short-term debt | Senior long-term debt |
|------------------------------|-----------------|-----------------------|
| Moody's Investors Service | P-1 | Aa2 |
| Standard & Poor's | A-1+ | AA- |
| Fitch Ratings | F1+ | AA |
| Dominion Bond Rating Service | R-1 | AA(low) |

La Banque Royale publie aussi son
Rapport annuel en français.



This annual report is printed on acid-free
paper and the entire book is recyclable.

Legal Deposit, fourth quarter, 2002
Bibliothèque nationale du Québec

Information contained in or otherwise accessible through the Web sites mentioned in this annual report does not form a part of this annual report. All references in this annual report to Web sites are inactive textual references and are for your information only.

Trade-marks used in this report include the LION & GLOBE Symbol, ROYAL BANK OF CANADA, RBC, RBC FINANCIAL GROUP, RBC BANKING, RBC ROYAL BANK OF CANADA, RBC ROYAL BANK, RBC INVESTMENTS, RBC INSURANCE, RBC CAPITAL MARKETS, RBC GLOBAL SERVICES, RBC BUILDER FINANCE, RBC CENTURA, RBC DAIN RAUSCHER, RBC LIBERTY INSURANCE, RBC MORTGAGE, RBC ADVISOR FUNDS, RBC ACTION DIRECT, RBC CAPITAL TRUST, RBC CENTER, RBC GLOBAL ASSET MANAGEMENT, RBC FUNDS, RBC GLOBAL PRIVATE BANKING, RBC GLOBAL INVESTMENT MANAGEMENT, RBC INVESTMENTS PRIVATE PLANNING, RBC INVESTMENTS FOCUS LIST TRUST, RBC LinC, RBC-OVERDRIVE, ROYAL MUTUAL FUNDS, ROYAL TAX MANAGED RETURN FUND, RBC.COM, ROYALBANK.COM, RBCINSURANCE.COM, RBCCM.COM, CASH & SAVE, FX DIRECT and PAYTICKETS.CA, which are trade-marks of Royal Bank of Canada used by Royal Bank of Canada and/or its subsidiaries. All other trade-marks mentioned in this report are the property of their respective holders, including without limiting the generality of the foregoing, the trade-mark Moneris Solutions etc., which are trade-marks owned by their respective third-party holders.

